The Institute of Chartered Accountants in England & Wales

Faculty of Finance and Management

Finance & Management

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What's in and what's out

Darrell Rigby's guide to the top management techniques favoured by big business

page 3

COMPANY LAW

Why 'corporate killing' is not the answer

page 6

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New 'update' articles in *F&M*

Much of the finance director's time is spent on non-financial activities, such as working with marketing people, using their softer skills in people management, developing strategies and generally creating value.

Consequently the Faculty has helped to bring and keep our members up to date in a broad range of management skills, especially those in which members may not have received formal training.

However, members often say that what they would also like from the Faculty is some form of 'update' service, making them aware of subjects such as tax, financial reporting and other technical areas falling into the domain of the finance director, though they may fall outside the domain of this Faculty.

We have therefore invited a number of specialists to contribute some regular 'update' columns to *Finance & Management* about major issues in their area.

We will provide the forum for an 'alert' about the particular subject, eg treasury, tax, financial reporting, strategy and so on – and the reader can decide whether to follow the issue up elsewhere.

To start the process, Francesca Lagerberg, senior technical manager for the Institute's Tax Faculty, has agreed to write the first update about taxation (*see page 12*).

We asked her to write on those current issues that are relevant to the finance director or the financial controller – and she has chosen to highlight double taxation relief and IR35.

Please let us know if you would like Francesca to provide an update in any other area of tax. Email: CDJackson@icaew.co.uk.

We plan to cover financial reporting next month.

November 2000 Issue 69

ABSTRACTS FROM LIBCAT

Barrow C – Phasing the facts

Director, Vol.54. No.2. September 2000: p76-80 (3 pages)

● *Dot-com directors in difficulty can learn from old-economy management tools. The author offers a survival guide for the first five stages of company growth. The five phases covered are: growth through creativity; through direction; through delegation; through co-ordination; and through collaboration.*

Ogley A – Holding companies

Tax Adviser, August 2000: p18-20 (3 pages)

● *The location of an ultimate holding company usually reflects the 'accident of its birth'. The company is formed where its founders happen to live and usually expands from that base. Once a company is successful, it may be impractical to relocate. Where the test of corporate residence for tax purposes is determined by the place of incorporation, relocation may prove difficult, if not impossible. Where this is based on 'effective management', the existing social ties of the senior management may lock it into the country in which it was established. This article discusses: the use of an intermediate holding company; reducing withholding taxes suffered; anti-treaty shopping rulings; general limitation of treaty benefits provisions; and the Netherlands and the characteristics of an ideal holding company location.*

Aveyard P – As inevitable as death: what general managers need to know about taxing e-commerce

Journal of General Management, Vol.25. No.4. Summer 2000: p38-50 (13 pages)

● *When governments get round to taxing the internet, the implications will be widespread. The authors discuss: taxable activities; understanding the tax implications of the internet: a primer for the general manager; potential tax losses for authorities; business concerns about e-commerce taxation, consumers and customers; technological features of the internet; general tax principles; future tax framework; e-commerce and tax – a tale of two countries (US and South Africa); and to tax or not to tax?*

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

These abstracts are taken from the ICAEW Library catalogue, LibCat, which is accessible from the Library's web site. Books can be lent (by post) to ICAEW members and photocopies can be supplied, at a reasonable charge, within the limits of the copyright laws. Further information about Library services (including access for non-members) can also be found on the web site.

Trusted management tool... or futile fad?

Management consultants, as a rule, focus more on promoting the latest tool or technique than on analysing its effectiveness. But for the past six years, US consultancy Bain & Co has been making just such an evaluation, reporting the views of senior executives of large companies on which tools work for them. This year, in the report produced by Bain's **Darrell Rigby**, there have been some startling findings. Helen Fearnley reports.

Unlikely as it may seem, there now exists a sort of Which? report on management tools and techniques. Once managements had to subscribe to a technique – be it JIT, TQM, or benchmarking – solely on the strength of the intellectual arguments put in its favour. Now, they have access to the views of those who have actually road-tested that technique. And in some cases the practical benefits fall far short of the promises.

Large companies' views on management tools

The source of this invaluable feedback on management tools is the global annual study 'Management tools and techniques', produced by Darrell Rigby, head of techniques research at leading US management consultancy Bain & Co. The report is based on comments from a random selection of senior executives of large companies, asked for their views of techniques currently in vogue.

The latest such report, published earlier this year, collates the views of business leaders in 475 global companies, and makes quite disturbing reading. Among its more negative findings are:

- that 46% of North American companies attempting real options analysis (which uses highbrow financial techniques to price share options in assessing the value of business investments) gave up the unequal struggle;
- that the much-promoted practice of knowledge management has also been less than an overwhelming practical success in North America (a frequently cited flaw being employees' resistance to surrendering their most valuable asset for the corporate good);
- that business process re-engineering no longer impresses users, its frequent consequence – the decimation of middle-management – having spawned the now greater fear of 'corporate anorexia' and skills shortages; and
- that two thirds of the 25 tools studied have declined in usage since the previous report.

However, the message is not entirely of doom and gloom. Some tools and techniques are rated more highly than those above. Of the companies surveyed:

- 81% happily employ strategic planning;
- 79% similarly use mission or vision statements; and
- 77% espouse benchmarking.

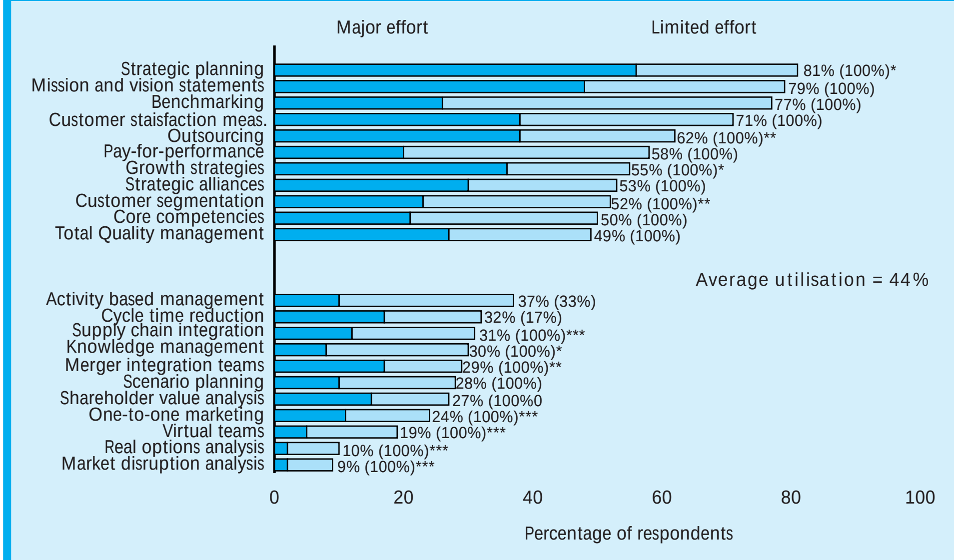
Too busy for new tools

Nevertheless, the general indication is that business leaders are spending less time on new tools and techniques. And this shift seems not merely because they have already integrated them into everyday management, nor even because the jargon-speaking and fashion-following elements accompanying adoption of such tools have palled.

Instead, follow-up interviews with the senior executives indicate that they are simply too preoccupied with getting to grips with the new economy and the challenges arising from the internet, to be busy implementing new tools and techniques.

Asked about the decline in use of tools – with 16 of the 25 tracked showing a decrease in reported use compared with the previous year – respondents blamed the current fast pace of business which makes it more practical to stick to the tried and true methods of management.

FIGURE 1 TOOLS UTILISATION RATES WORLDWIDE



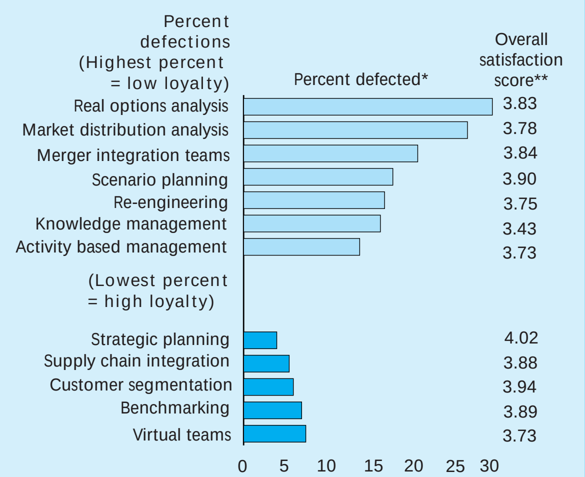
( )Signify the percentage of years this tool has been significantly above/below the mean; *Tool introduced in 1996; **Tool introduced in 1998; ***Tool introduced in 1999. Note: only tools significantly above/below the average utilisation (95% confidence) are listed; dark shadowing indicates major efforts; light shade indicated limited efforts. Source: 1999 Worldwide Survey.

Narrowing the field and spotting the best/worst runners

Of course, the term management tool covers a wide range of approaches to management, from simple planning software to revised philosophies of the business world. In fact there are some 100 recorded management techniques in use. And many such tools offer conflicting advice – one, for example, advising retaining all your customers, while another recommends concentrating only on the most profitable. But their common feature is the promise they hold of a more successful business – a promise managers have, until now, found irresistible.

As already mentioned, the Bain study looks at just 25 techniques (and geographical analysis shows this narrowing of the field to be sensible, since even in Brazil – the world's most eclectic user of management techniques – the average number of tools used is only 13.1, while the worldwide average is a mere 10.9).

FIGURE 2 LOYALTY TO TOOLS VARIES GREATLY



*Tool used in past 5 years but not in 1999; **Satisfaction scale from 1-5.
Source: 1999 Worldwide Survey.

Looking at the utilisation, worldwide, of specific tools (see Figure 1 – showing those tools significantly above and below average), strategic planning, mission and vision statements, and benchmarking are clear winners – and have been for some years. (Benchmarking tops the poll in Europe, as in the preceding years, while in North America strategic planning is the clear winner, used by 89% of companies.)

What comes as a surprise, however, is the comparatively low utilisation of the likes of knowledge management – admittedly a relative newcomer as a technique – as well as the longer-established shareholder value analysis and scenario planning.

The top 10

The latest Bain report finds that the 10 most popular tools have a trusted-and-true element, all having been used by 50% or more of companies surveyed in each year since these reports began.

These top 10 techniques are, in descending order: pay-for-performance; cycle time reduction; strategic planning; mission and vision statements; customer satisfaction measurement; growth strategies; customer segmentation; total quality management; one-to-one marketing; and scenario planning.

But over all 25 tools, such a level of loyalty was sometimes lacking. Rating this quality by the percentage of companies which stopped using a tool in 1999, after using it at least once in the previous five years, Bain found (Figure 2) that some of the recently most strongly-promoted tools (eg real options analysis, re-engineering, knowledge management, activity based management) have low loyalty ratings.

However, as Rigby points out in his report, defection is not necessarily a reflection on the tool, which might have fulfilled a relatively short-term purpose, or may no longer be appropriate to the company's needs. Hence the satisfaction ratings (Figure 2 again) are in some cases as high for tools with a high defection rate as for those inspiring great loyalty (eg scenario planning and benchmarking, respectively).

FIGURE 3 THE BEST TOOLS FOR THE JOB

● = consistently the best tool for the job
○ = often the best tool for the job

	Financial results	Customer equity	Performance capabilities	Competitive positioning	Organisational integration
Balanced scorecard*					○
Core competencies			●		
Customer retention		●			
Customer satisfaction		●		●	
Customer segmentation**		●		○	
Cycle time reduction	●	○	○		
Growth strategies*	○				
Mission and vision statements					
One-to-one marketing***		●			
Outsourcing**	●				
Pay-for-performance	○				
Shareholder value analysis	○				
Strategic alliances		○		●	
Strategic planning*	●		●	●	●
Supply chain integration***	●		●	●	○
Total quality management		●		○	○
Virtual teams***					●

*Tool introduced in 1996; **Tool introduced in 1998; ***Tool introduced in 1990. Source: 1994-1999 World Survey

Satisfaction levels for the tools were, on the whole, mildly positive at an average 3.87 out of a possible score of 5 (for highly satisfied). At the two ends of the scale one-to-one marketing made its debut as a tool with a very high satisfaction rating (4.03), while knowledge management scored extremely low (3.43).

Follow-up interviews indicated that the two most common reasons for dropping a tool were either its expense outweighing the benefits, or lack of management/employee support for the tool. Indeed, 95% of respondents felt that tools require top-down support to succeed.

Other useful insights from these interviews included that a high proportion (82%) believe that companies that use the right tools are more likely to succeed, and that the respondents tend to use successful tools over and over again (80%).

Major efforts achieve better satisfaction

For all the tools studied, the best results came where a major effort had been put into adopting the given tool. Rigby even goes as far as to suggest that some tools are not appropriate for use on a limited basis – singling out market disruption analysis as one giving a relatively poor satisfaction level when used on a limited basis. However, some can produce reasonable results even on a limited adoption basis – a good example being cycle time reduction.

Same favourites – differing corporate success levels

Interestingly, the Bain report finds that the 10 top tools are almost identical for successful and non-successful companies, the difference being – perhaps unsurprisingly – that the successful companies are generally more satisfied with the tools they use.

The discrepancy in successful company/ unsuccessful company satisfaction levels is particularly marked for such techniques as pay-for-performance, strategic planning, customer satisfaction measurement, growth strategies and scenario planning.

The best tools for the job

As Rigby concludes, very few tools exist which do it all, the trick being to choose the best one for a specific job. As shown in Figure 3 – featuring shaded circles for areas in which a given tool has been either often or consistently the best tool for the job – most tools score highly in only one or two performance categories. Only newcomer supply chain integration and the perennial strategic planning score strongly in four of the five performance areas.

Finally, he offers some refreshingly objective advice on using tools:

1. *get the facts* – every tool has a set of strengths and weaknesses. Success depends on combining the right tools in the right ways at the right time. Talk to other users;
2. *champion enduring strategies, not fleeting fads* (which, anyway, tend to result in loss of employee confidence) – concentrate on realistic and strategic directions, while regarding the tools for achieving them as expendable;
3. *choose the best tools for the job* (ones which discover unmet customer needs) – build distinct capabilities, exploit competitor vulnerabilities, and develop breakthrough strategies by integrating these accomplishments; and
4. *adapt tools to your business system* – rather than vice versa.

Bain & Co is a US management consultancy. The latest 'Management tools and techniques' survey can be downloaded from the Bain web site: www.bain.com

'Corporate killing' is not the answer

The Institute is not convinced by the government's proposals for reforming the law of involuntary manslaughter – in particular, the plan to introduce the concept of corporate responsibility for death following accident or disaster.

Felicity Banks of the Institute's Business Law Group explains why.

What government action would best avoid the kind of public outcry that followed recent major disasters such as the sinking of the Herald of Free Enterprise or the Paddington rail crash? 'Put those responsible in jail for a long time' seems to be the one the government favours, with little thought as to whether a simpler and less legalistic set of reforms might be better.

Following a Law Commission report, the government has published proposals for the reform of the law of involuntary manslaughter – that is, the offences which are committed when a death is caused by some action or neglect on the part of a person who does not intend to kill the victim. The reforms are undoubtedly needed. Much of the current law on manslaughter depends on the common law and is so imprecise that judges have a hard time instructing juries.

Responsibility

The problem the Institute has been addressing in its response to the proposals rests not in the question of manslaughter as committed by individuals, but in corporate responsibility for death following accident or disaster.

The government is consulting on two main proposals. The first is its firm intention to introduce a new offence of corporate killing, to make it easier for blame to be laid at the door of a corporate body, wherever death has been caused by management failure on the part of an organisation. Second, it is consulting over whether to provide that an individual who can be shown to have had some influence on the management failure should themselves be guilty of an offence, punishable by imprisonment.

The government, justifying its proposals, lists a number of recent rail and ferry disasters, where serious loss of life resulted. It does not, however, list a single air disaster, in spite of the propensity of the air transport industry to result in occasional disasters involving even more serious loss of life.

This is no coincidence. The air transport industry has two advantages over the other means of transport: a rapid and dependable system of no-fault investigations and universal payment of generous compensation where death or injury has occurred.

Investigations are carried out on the same basis for both near misses and actual disasters and mean that repeat incidents are minimised. In addition, a dependable source of explanations is available to relatives along with generous compensation sparing them the feeling of injustice and evasion arising from inadequate compensation, paid after substantial delay.

This can only be achieved by carrying out investigations on a 'no fault' basis, as there is no incentive to tell the truth where a serious criminal conviction is likely to be the result. Similarly, if compensation is invariably paid on a no fault basis, no-one will delay payment for fear that it appears an admission of guilt.

Weaknesses

It cannot be denied that such events as the sinking of the Herald of Free Enterprise and the Paddington crash almost certainly did reflect significant weaknesses in the health and safety cultures of the businesses involved, nor that it is the responsibility of boards of directors to make sure appropriate systems are in place. These should use smaller accidents and near misses as warning signals, and prompt action should be taken following them.

But the government's proposals are presented in the context of manslaughter alone. No consideration is given to what other sanctions could be taken, for instance where management failure leads to injury, but death is avoided. Deaths are in fact uncommon, whereas many organisations can be casual about health and safety. To punish the uncommon result, without taking any action against the more frequent, leads to a lottery effect where a very few offenders are likely to be severely treated while the majority go unpunished.

The government should be doing everything it can to reduce the likelihood of fatal accidents and, where they do occur, to ensure the rapid and certain provision of explanations and appropriate compensation. The Institute is of the firm opinion that the appropriate way for this to be done is by a strengthening of the health and safety legislation, and the introduction of no-fault systems of investigation not only for actual disasters, but also for smaller accidents and where disasters have been narrowly avoided.

Introducing the kind of Draconian penalties proposed will do even more to ensure that anyone involved in the run up to a disaster does everything possible to minimise the blame laid at his door and nothing to help the emergence of the truth.

Commercial, not criminal, sanctions should punish organisations which fail in their responsibilities. And these should be applied by customers appropriately appalled by past disasters and able to use their market power to refuse to buy from those responsible.

Where is PanAm now, after it failed in the security procedures that would have avoided the Lockerbie disaster?

Felicity Banks is a member of the Institute's Business Law Group.The full text of the Institute's response to the government proposals on manslaughter are available as technical release TECH 26/00, available from www.icaew.co.uk.

The Faculty would like to hear from members with views on this subject – see contact details on page 2.

Disability law – the implications for employers

Recent changes in the law on disability discrimination have caused some businesses concern over the extra administrative burden involved. **Andrew Payne**, of solicitors Lovells, explains what exactly the changes entail.

The new Disability Discrimination Act (the Act) makes it unlawful for employers with 15 or more employees to discriminate against a disabled person in terms of recruitment or dismissal, training, promotion, benefits or terms of employment or by subjecting the disabled person to any other detriment.

The implications of this cannot safely be ignored. Disabled people represent 11% of all people in employment, and increasing numbers of claims are being made to employment tribunals alleging disability discrimination. Employers therefore need to understand their duties under the Act – not least because tribunals can award unlimited sums in compensation. This article seeks to draw the reader's attention to a number of important points relating to the Act.

A broad definition of disability

The Act states that a person has a disability if he has a 'physical or mental impairment which has a substantial and long term adverse effect on his ability to carry out normal day-to-day activities'. However, the definition and its application in practice are complex.

In the first instance, it is important to note that the Act covers more people than just those who are registered as disabled. For example, people with sensory impairments, clinically well recognised mental illnesses, learning difficulties, dyslexia or mobility impairments are likely to fall within the definition.

It is also likely that those suffering from work related stress and ME will fall within the definition. Further, the Act protects those who were disabled in the past but who no longer suffer from the impairment.

Two forms of discrimination

An employer might discriminate in one of two ways:

1. By less favourable treatment.

This occurs where, for a reason which relates to a person's disability the employer treats that disabled person less favourably than someone to whom that reason does not apply, and the employer cannot show that the treatment is justified.

In practice it has been found to be less favourable treatment to dismiss someone for being off work due to a disability even when a person who had been away from work for the same time but not for a disability reason would have been treated the same.

Thus less favourable treatment may not be difficult to prove and, from the employer's point of view, reliance will have to be placed upon the justification. But discrimination will only be justified if the reason for it is both material to the circumstances of the case and is substantial rather than minor or trivial. An employer may, for example, be able to justify the dismissal of a disabled person who has been off work for a long time on the grounds that he is unable to carry out any part of his contract.

2. Through failure to make reasonable adjustment.

The second way in which an employer may discriminate is by failing to comply with the duty to make a reasonable adjustment to arrangements or physical features of the employer's premises which place the disabled person at a substantial disadvantage, where such failure is not justified. Again, the reason for the failure must be material and substantial.

Employer's knowledge

An employer cannot claim that there was no 'less favourable treatment' because he did not know about the employee's disability.

However, an employer's knowledge is relevant to the duty to make a 'reasonable adjustment'. The duty only arises if the employer was aware or could reasonably be expected to be aware that the person had a disability. However, if the employer attempted to claim lack of awareness, he would need to show that that lack of awareness had been widespread throughout the business since, under the Act, the knowledge of employees and agents will be imputed to the employer. For example, the knowledge of an occupational health officer may be imputed to the employer so that an employer will be required to make a reasonable adjustment even if the reasons for it remain confidential.

Employer's liability

Part-timers and temporary employees are also covered by the Act, such contract workers being covered by treating the person to whom the worker is supplied as an employer. Employers are, additionally, responsible for the actions of their employees done in the course of contract workers' employment, and should therefore make it clear to staff that it is unlawful to discriminate against disabled people. They should modify grievance and disciplinary procedures and consider providing disability awareness courses.

It is not possible for employers to exclude their liability under the Act but disability discrimination claims can be included in compromise agreements and ACAS settlements.

Reasonable adjustments

The duty to make 'reasonable adjustments' is a cornerstone of the Act. It is also a duty that employers should keep under constant review as further or different adjustments may be required in the future. This duty includes altering the physical features of premises (for example widening doors, building ramps, altering the height of light switches and altering paint schemes) even where the employer only leases the building.

Tribunals will expect the employer to have enquired whether financial assistance is available from the government or voluntary bodies

Adjustments may also have to be made to work arrangements. These may involve re-allocating duties, altering working hours, re-assigning workplaces, providing a reader or interpreter and acquiring or modifying equipment.

As to what is 'reasonable', considerations include the effectiveness of the step, the practicality of the step, the disruption that will be caused to the employer and the financial costs. It would not be unreasonable to have to spend what it would cost to recruit a replacement for the disabled person. Tribunals will expect the employers to have enquired whether financial assistance is available from the government or voluntary bodies.

Recruitment and promotion

Employers must take care to avoid discrimination in the job specification, the job advertisement, and the selection process. Adjustments may be required to the location and timing of interviews, assessment techniques, interviewing, and the selection criteria. For example, recruitment information may need to be provided in alternative formats (like braille or large print) or an applicant with a learning disability may need to bring a friend to the interview. Aptitude tests may need to be adjusted so that they do not place a disabled person at a disadvantage. Care must also be taken when asking a disabled candidate to undertake a medical examination. Consideration may also need to be given to allowing applications to be received in different formats – for example on tape or typed instead of written.

Similar points can be made in relation to promotion. An employer may have to make adjustments to the selection process and the new job itself. However, there is no requirement for an employer to treat a disabled person more favourably than he treats others.

Termination of employment

The Act does not prevent a disabled person from being dismissed. Dismissal of a disabled person for a disability related reason would need to be justified and the reason for dismissal must be one which could not be removed by a 'reasonable adjustment'. However, there is no requirement to create a post especially for a disabled person in order to avoid dismissal. In some circumstances a reasonable adjustment may be to offer the disabled person a different position even if this is a lower paid job. When selecting employees for redundancy it is important that the criteria for selection do not discriminate against disabled people. A tribunal awarded one employee who was discriminated against in the redundancy process over £100,000 in compensation.

Conclusion

Experience to date shows that employers need to manage issues arising from disability in a co-operative and flexible way. Those involved in staff management and supervision should be made aware of disability issues. It is important not to make assumptions about the needs and problems that disabled people face. Employers sometimes forget that in many cases the best person to speak to is the disabled person himself. However, they should be prepared to seek professional advice if necessary.

Andrew Payne is a lawyer in the employment group at Lovells, tel: 020 7296 2000; fax: 020 7296 2001; email:andrew.payne@lovells.com.

The firm's web site is at: www.lovells.com Lovells (the merged firm of Lovell White Durrant and Boesebeck Droste, practising as Lovells Boesebeck Droste in some jurisdictions) is an international law firm.

Trying to keep the customer satisfied

The importance of adding value for all stakeholders in a business is accepted, but how can management tell exactly what customers want? **David Shoesmith**, managing director of Halifax-based Abram Pulman Steel, found a new customer survey technique provided unsuspected insights. Helen Fearnley reports.

A perennial problem for businesses is assessing customers' satisfaction levels and their needs. Conventional methods of survey tend to elicit responses only from the highly satisfied or the very disgruntled. But now it is possible to get a more complete view of customers' requirements.

Halifax-based steel stockholding company Abram Pulman Steel was one of the first to use this method – already popular in the US but relatively new in Europe. As a result, says managing director David Shoesmith, "Since the survey, we have been very successful in increasing our business and we are currently having to look at different working hours and increasing staff levels to meet demand. Indeed, just eight months after the new style survey, internal accounts show the business is looking at a 30% increase in annual turnover."

John Coldwell, the business consultant who recently negotiated the European licensing rights to this InfoQuest Business Process Review system, says he deliberately chose Abram Pulman Steel as a particularly challenging early participant because it deals in steel, rather than anything remotely 'sexy' or 'soft', so its customers are not generally given to navel-gazing about ways of improving their lot.

The results were surprising. Although David and his fellow director Chris Horner had assumed that customers were buying from them solely on price, many of them said that although price was important customer service was a key selling point.

Or as David puts it, "All customers are very price conscious, but those surveyed considered our service to be equally important." Armed with this insight, David and Chris encouraged staff to build on these service strengths.

Worldwide results

Collating the results from InfoQuest's surveys on behalf of some 20,000 companies in 40 countries, some interesting generalisations emerge, including that:

- a 'totally satisfied' customer contributes 2.6 times as much revenue as a 'somewhat satisfied' customer, and 17 times as much as a 'somewhat dissatisfied' customer; and
- a 'totally dissatisfied' customer decreases revenue at a rate equal to 1.8 times the positive revenue contribution made by a 'totally satisfied' customer.

This last finding is particularly worrying since it means that even with twice as many totally satisfied as completely dissatisfied customers, the business would be doing little better than standing still.

How it works

The InfoQuest system has a particularly high response rate (75%), perhaps substantially achieved because the survey is not a box-ticking exercise, but involves a segmented box, each segment containing a question plus strips of paper bearing potential answers – one of which the respondent posts into a slot in that segment of the box. Apparently this method has far more appeal to busy managers than receiving yet another form to fill in.

Companies must have at least 60 significant customers or economic buyers to provide a sensible volume of respondents, and these customers are contacted discreetly to ensure they are happy to participate. After that, InfoQuest monitors the replies until 75% have been received, then sends them off for analysis.

The result

The survey certainly worked for David Shoesmith and Chris Horner, who have decided to change the century-old company ethos to concentrate on marketing and advertising. "We've decided to change tack, raise our profile, and get our name out there. These are exciting times at Abram Pulman Steel," says David Shoesmith.

More information on InfoQuest can be obtained from John Coldwell, tel: 01484 864883; email jc@infoquestcrm.co.uk; or visit the web site at www.infoquestcrm.co.uk.

Treasury matters

Chris Mansell reviews current treasury-related issues.

Managing energy costs

September's oil blockade will have prompted risk reassessments by many businesses. Action in managing risks however can be positively dangerous unless conducted in a very structured context.

In the case of energy costs, like foreign exchange, there are commodity markets and corresponding instruments available to help manage the dual risks of price volatility and breakdown in supply. The approach is very similar to addressing financial risks, ie by assessing:

(a) what are the price risks and where they arise;
(b) how significant they are in terms of costs and revenues;
(c) to what extent these risks can be passed on or correlated with pricing strategy, the objective for most companies being the stabilisation of margins in the face of pricing and margin risk;
(d) how the risk management objectives should be expressed;
(e) what is the organisation's appetite for self-insuring (offloading risk has a cost, like insurance); and
(f) what controls are required once the programme is in place.

The International Petroleum Exchange (IPE) is Europe's leading futures and options exchange; it provides a regulated market place where industry participants can manage their exposure to energy prices. Contract formats are standardised and the obligations of members are guaranteed by the London Clearing House. The alternative is the bilateral over-the-counter (OTC) market where bespoke contracts can be constructed to respond to the needs of any situation. The traded instruments are therefore relatively informal, unregulated contracts and the market has no real transparency or indeed liquidity. For those outside the energy industry (notably in transport) high certainty on price is worth paying for. Futures can achieve this.

Energy risk management might be considered by any organisation where energy represents a high proportion of the overall cost structure. There are consultants, such as the London-based, Petroleum Economics, who are experienced in matching available instruments to an organisation's real needs and giving an authoritative view on how effective the risk management programme might be. However, finance managers, used to a relatively smooth ride in dealing in financial markets, should be prepared for turbulence.

The debate about financial services

LETTER FROM BRUSSELS

by
Martin Manuzi

The financial services sector in Europe is racing ahead, powered by the development of internet technology, an increase in on-line brokerage, e-banking, electronic clearing networks and so on. Unfortunately, the European Union is struggling to keep up.

The idea of creating a single European market for financial services has existed for many years. But the euro has provided a significant fillip to the idea: creating a modern financial architecture alongside a common currency which will reduce the cost of capital and financial intermediation to a minimum. However, the financial services sector remains segmented – some 50 different bodies within the EU have supervisory responsibilities, and the UK is the only country to have attempted rationalisation.

While speed is essential in financial services, the EU's legislative process is the very antithesis of this. However, the real problem is not simply that regulations and directives take a long time to develop and implement, but that there is no agreement over the future political shape of Europe.

Unthinkable

At a gathering of EU policy-makers in Paris a few weeks ago, an American solution to the regulation of Europe's financial markets was raised – a European Securities and Exchange Commission. In reality, however, the prospect of a single regulatory authority is politically unthinkable. The Danish referendum result on the euro underlined the fact that there is unlikely to be sufficient political consensus to undertake such an initiative, though it has also increased awareness of the need for reform.

To this end, the EU is seeking to move forward on the basis of an ambitious 'Action Plan for Financial Services'. Formally adopted last December, this aims to create an integrated financial services sector by 2005. Just as with the EU writ large, this integration will necessarily be a mixture of greater co-ordination between member states and the establishment of some pan-European capacities – all of which will necessarily raise questions over subsidiarity and national sovereignty.

Discussions on the imminent approval of a European Commission proposal on the opening of pension markets in Europe, one of the pillars of the Action Plan, illustrate the degree of pragmatism which will be required. The liberalisation of this politically sensitive sector has encountered considerable opposition from certain states fearful of losing control over a crucial 'national competence'.

Brussels appears to understand that the market won't wait: whether the member states do is a different matter.

FORTHCOMING FACULTY EVENTS

- **20 February 2001**
  LECTURE
  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 6.00pm; lecture 6.30pm and buffet 7.30pm.

***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'. His latest book, 'New Economy – New Competition' is due to be published in 2001. His next book, 'Strategy & Capability', should be completed early in 2001. He is currently working on an industry-funded research project examining the drivers for competition and globalisation across a range of industries including domestic appliances, electrical products, professional service firms and telecoms. David has worked with the senior teams of a range of firms including Cornhill, Ernst & Young, Fujitsu/ICL, 3M, Marconi, Siemens Computer Systems, and Sun Microsystems. In addition, he has been an adviser to the Office of Fair Trading on competition policy and is currently an adviser to the government of Ethiopia. He is also an advisor to the World Bank on designing technology-based distance learning in developing countries. Prior to his academic career David worked for a merchant bank and a firm of management consultants.*

- **13 March 2001**
  LECTURE
  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 6.00pm; lecture 6.30pm and buffet 7.30pm.

***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. Mark has advised businesses across Europe and in the US in a range of industries. Before joining PA, Mark was director of corporate development for UniChem. Mark has an MA in mathematics from Cambridge University and is an associate fellow of the Institute of Mathematics and its Applications.*

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

Tax update

In the first of a planned series of regular columns in *Finance & Management*, **Francesca Lagerberg**, senior technical manager of the ICAEW Tax Faculty, examines two issues which have dominated the corporate tax world this year: the changes to double taxation relief and the implications of the new rules affecting those who provide personal services via an intermediary (better known as IR35).

Double taxation relief

With a short postponement, rather than a major re-think, on the new proposals for double taxation relief, this issue is still very much under review. The August issue of the Revenue's *Tax Bulletin* noted that Revenue worked examples and details of the consultation on in-country mixing and group surrenders would be available by the end of September 2000.

They were not released at the time of writing but keep an eye on the Revenue's web site (www.inlandrevenue.gov.uk) for details. The Revenue has also noted that it is keen to expand its guidance in this area. If you have points which you believe require clarification and would be of wider interest, you can contact Susan New, International Division, Room 304, Victory House, 30 - 34 Kingsway, London WC2B 6ES or telephone: 020 7438 7250.

Providing services (IR35)

On the issue of IR35, there are some potential 'elephant traps' in the corporate field that are worth being very aware of. The new rules introduce a 'deemed' or notional salary on those who have relevant engagements under the legislation found in section 60 and Schedule 12 to the Finance Act 2000. A deduction is given for corporation tax and a relief for income tax for the amount of the notional payment and related employer's National Insurance Contribution (NIC). This is given as a deduction in calculating the intermediaries' business profits.

Any deduction in calculating the profits for corporation tax or for Schedule D purposes will be given in the period of account in which the Schedule E payment is treated as paid. There is no other mechanism given for deemed payment deductions. This causes difficult and complex timing problems.

For example, assume a company has a 31 March year-end and makes a deemed payment at 5 April following its accounting period. The deduction will not be given for the deemed payment in its 31 March accounts even if the 'deemed salary' were then to be actually paid on, say, 30 April. Therefore, if the notional salary payment was calculated on 5 April 2001, in this case it would not be allowable as a deduction until the year to 31 March 2002.

There are a number of possible solutions:

a) the company could change its year-end to 5 April or later, so that the notional payment date falls into the period of account; or
b) alternatively, the company could calculate salary on a monthly basis and pay it as actual salary.

The latter is the Revenue's preferred choice but may be neither practical nor sensible if the company is concerned about its cashflow.

The company could look to calculate the notional salary immediately before the year end and make an actual salary payment of the equivalent amount. Again this may not be practical.

The Tax Faculty has a questions and answers helpsheet on IR35 (Tax Guide 6/00) available on its web site (www.taxfac.co.uk). There is also a useful demonstration of the corporate implications of IR35 on the Accounting web site (www.accountingweb.co.uk).

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