Finance & Management

November 2002 Issue 93

The monthly newsletter for members, with news, views and updates on current topics.

THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND & WALES

Faculty of Finance and Management

'THERE IS NO MONEY IN POETRY, BUT THEN THERE'S NO POETRY IN MONEY EITHER... ' – Robert Graves

Intellectual capital

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FORTHCOMING EVENT ...

Leadership

7 November – In a Faculty evening lecture, Steven Sonsino, a fellow of the Centre for Management Development at London Business School, will discuss 'Leadership unplugged – a new role for the finance director'.

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What's in a (corporate) name...

Recently, many changes to established corporate names have been criticised as expensive 'window dressing' – yet such expenditure must have been signed off by a finance director. What persuades a hard-nosed 'figures person' to sanction heavy investment in cosmetic change? Helen Fearnley reports.

Corus, Marconi, O2, Monday (almost), Consignia (briefly) – sometimes it seems the entire business world has succumbed to a corporate-strain of Bridget Jones-ism in its fevered conviction that a change of name will right all reputational wrongs.

But surprisingly, given the widespread impression that this is a burgeoning practice, research by one of the leading brand and identity consultancies shows this passion for name changing has actually recently declined.

The latest (33rd) semi-annual survey of corporate name changes by brand and image experts Enterprise IG shows that in the first half of 2002 there was a 30% decline – from 1,993 to 1,397 – compared with the first six months of 2001. This was the most dramatic decline in such name changes for two decades.

See also Alan Mitchell's Marketing Update column on page 13
'To rename, or not to rename... '

Encouragingly, this sharp fall does not represent loss of faith in the importance of a name (the survey revealing growing recognition of the marketing significance of the corporate name) but, rather, a decline in what are deemed 'frivolous' changes.

Instead, the majority of early 2002 corporate name changes stemmed from well-known companies streamlining existing names or changing to ones more appropriate to current and future operations and the majority (60%) resulted from restructuring such as mergers, acquisitions, divestitures, sale of assets and spin-offs.

Not that most of the recent name changers would deny a smidgen of transformational aspiration in their reasoning for the change – a desire to adopt a more attractive identity, at a stroke.

Nevertheless, as experts in the image industry emphasise, for a fair number

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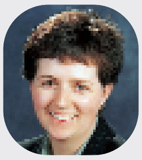

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Corporate names – *from page 1*

there were reasons far less pie-in-the-sky. Accenture, for example, was perfectly happy – and extremely well-regarded – in its former incarnation as Andersen Consulting. Only at the insistence of former parent Arthur Andersen was the newly-independent consulting business legally obliged to lose the 'Andersen' element by a fixed date.

This change could have been a disaster, with years of invested value and reputation associated with the Andersen Consulting name jettisoned overnight. As it happened, seven months after the switch – and after spending in the region of $100 million – Accenture had the highest brand recognition of any management consultancy in the world and was judged 'best US new identity of all time'. Additionally, with the benefit of hindsight, its change of name looks particularly fortuitous.

Genuine motivating factor

Indeed, closer inspection reveals that the managements of practically all of the renamed concerns attracting public attention can cite some genuine motivating factor(s).

The erstwhile British Airways, now BA, had experienced a genuine problem with customer perception – the 'British' signalling a domestic airline when it was in fact already a serious global player.

Less felicitous – but still, arguably, rational – changes include the Post Office. The organisation had real issues with its evolving image. Was it domestic or international? Was it primarily delivering post to commercial enterprises, or trying to meet their broader overall communication requirements?

It felt the need for a different identity to reflect the organisational changes. Consignia was the proposed solution for the international business side – until public outcry undermined management's resolve.

Arcane choices

However, regardless of the commercial/conceptual imperative – and excepting the fairly logical BA name-change – the choice of new title frequently seems puzzling. Why opt for Corus, Consignia, Vivendi?

A corporate name change is confusing, as well as radical. Firstly, the change in most cases is signifying some switch in activities. Then, as the logo, fascias and letter-headings all change, there is no visual clue to the former identity. And finally, if the new name seems to bear no relation to the real world, there seems nothing to lodge it in the mind.

The clever bit

Yet, say the experts, that is exactly the clever bit: to slough off a negative image associated with the old business calls for brutal, not subtle, change. And what better than a so-far meaningless word to embrace a whole set of new activities? By forcing stakeholders to make this effortful mental 'break' with the old, the new identity is being rammed home and quite soon the new title will conjure up exactly what the organisation now represents.

> To slough off a negative image calls for brutal, not subtle, change

As Charlie Wrench, managing director of Landor Associates, the world's best known branding consultancy explains: "It is a misconception that a name has a great deal of meaning at its inception: that meaning becomes attached to the name over time. Initially there was nothing about the made-up names 'Kodak' and 'Bird's Eye' to convey film or frozen vegetables."

Names: a change that worked ...

Lose the bathwater, not the baby

However, a stark, association-breaking-and-remaking name change is not the only solution. A brand name takes time and money to build, and jettisoning it may mean throwing the baby out with the bathwater. A company must be very sure that it is not abandoning a name in which there is still positive equity value – one which could be made to embrace the planned change of direction.

When Landor, for example, was involved in the repositioning of France Telecom, France's domestic telephone company, it questioned whether a name change was the best device.

France Telecom was in the process of transforming itself into a global world player in telecommunications. Hence Landor needed to determine whether the France Telecom name could be successfully relinked to this new profile without being changed. Would consumers believe in France Telecom as a forward-thinking global hi-tech player, involved in IT and internet rather than terrestrial phone lines?

In any such exercise, the criterion is to establish how much the old name would undermine perception of the change in activity. The methodology is to issue 'proposition statements' of the new direction and proposed activities to 'samples' of the public. The results show how well a reframed – rather than renamed – identity sits with the public.

Economic modelling is also carried out to establish the relative costs of

... but no change needed here

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media investment for changing perceptions of the business with and without a name change.

In France Telecom's case, the brand was found to be sufficiently flexible to embrace the new direction, and retaining the name more economical than changing it.

Costly exercise

There is no disguising that name-changing is an expensive step. Even those in the business of facilitating such action advise caution. As Terry Tyrrell, chairman of Enterprise IG, puts it: "Changing your name is certainly something that shouldn't be entered lightly, from the expense point of view. Registration is generally the highest cost, and depending on how many – and which – markets you are registering in, this can run to millions of pounds for the largest portfolios.

"The European Community Trade Mark (CTM) has made it easier to register trade marks throughout the European Union. A central search for CTMs can be carried out on-line but to obtain a complete picture it is necessary to search the National Registries. As it is now possible to register almost anything as a trade mark (subject to distinctiveness and prior use requirements) so long as the proposed trade mark is 'capable of being represented graphically' it should in theory be easier to register a trade mark. The problem is, though, that as it is easier to register more varied things as trade marks so there are more applications to work around.

"Similarly, in North America, the US and Canadian registers are separate although it is possible to conduct a search under Compumark's SAEGIS database which should be conclusive in relation to both (and that includes Federal and State trade marks in the US). It must be remembered that unregistered marks will, of course, not be covered.

"As a rule, the less developed the place, the harder it is to do the search and to give an example the Greek, Irish and Portuguese registries must be searched manually because the databases are not yet fully computerised."

Further, Tyrrell points out: "Lawyers will charge fees for both the search of database (to ensure the name is not already registered) and for filing the actual registration.The registration fee includes not just a fee for the registration of the name, but also a charge for its registration in each of a number of

> Registration can run to millions of pounds

classes. For example, someone in the financial services sector may wish to protect its name by registering in the classes: banking; insurance services; and professional services.

"Take such fees per name and per class and per market, and the whole registration business becomes highly costly."

Landor's Wrench expands on that view. "There are trademark, copyright and linguistic limitations on the choice of name. Taking the linguistics first, a car cannot be named 'Nova' if you hope to market it internationally, as nova is Spanish for 'doesn't go'. On the copyright and trademark side, a truly global operation might be involved in over 200 markets around the world, and in any one of those the name you would like may have been copyrighted or registered as a trademark by some concern, however small.

"As a rule of thumb, of 500 potential new names generated, roughly 480 will not be available for use. And of a bill of anything between £50,000 and £200,000 – depending on the size and reach of the company concerned – advisers may well only charge in the vicinity of 25% for the actual generation of a list of possible new names, and as much as 75% for the exploration and search involved in establishing which are free and most desirable for use."

Then there is the cost of advertising, not to mention physically switching names. Indeed, of the $100 million figure for Accenture's name-change operation, industry insiders reckon that only in the region of $500,000 would have gone on designing and registering the new choice, but roughly $25 million on physically changing the business's applications, and another $75 million on media campaigns. (To be strictly fair, they add, only about 40% of the spend on advertising and changing of applications would be beyond the consultancy's normal outlay.)

When it works – and when it doesn't

The success or otherwise of a name change depends on the reasons for doing it, and the way it is carried out.

However, of the wholesale switches of identity Tyrrell remarks: "I do feel that name changing has had something of a bad press lately. However, it is true that there are some irresponsible consultants giving advice not based on business rationale, who are trying to make their name at the big, bizarre end of the name-change field. They suggest ones with pretty flimsy justification.

"Accenture, on the other hand, was well-chosen. The firm picked it to suggest 'accent on the future'. Of course, one mustn't forget the practical limitations on names available. Almost every real word in Webster's English Dictionary is now 'taken', somewhere in the world."

> With the right delivery, a name change can be a positive exercise

On the implementation front, Consignia is, perhaps, a good example of poor delivery rather than flawed concept. According to Wrench, "in fact, 'Consignia' was a pretty good choice of name, with its links with 'consigning' or 'signalling'. But it seems management was so terrified of the media reaction that it chose to announce the change as something marginal and 'cheap', giving the impression it was acting on a whim.

"Changing the name for the international business was a good idea, and would not have affected people in the High Street, who would still have been dealing with the Post Office. Management just shouldn't have pussy-footed round the issue."

His verdict? With the right delivery – flagging the transformation both to the outside world and within the company – a name change can be a positive exercise.

Conclusion

The expense of a corporate name change may be non-negotiable, but its success (or otherwise) is more open to influence. Four factors make the difference between triumph and disaster. The first three – having a sound case; timing and executing the change intelligently and sensitively; and delivering the promised outcomes – are crucial.

Even so, the fourth – a not-too-ludicrous choice of name – makes stakeholder acceptance more likely. And, like it or not, one or two battle-scarred would-be name-changers will attest to the importance of that. **F&M**

Why a name-change can add up, financially

Where there is a need for a change of direction, any finance director worth his spreadsheet will be aware. He has probably authorised considerable amounts to be spent on marketing only to see sales slip year on year.

Advertising may be making no impact on return on sales. When that happens, something dramatic is required to get trade retailers to take a new look at what the company has on offer. Changing the corporate identity can provide that jolt.

If £10 million spent on a name change generates an inclination to take a new look at what a company is up to, and if that new look reveals a more attractive promise that had been overlooked, and that experience, multiplied across millions of customers' results in tens of millions of pounds more in profits, that is a relatively small price to pay.

Other reasons for making name-changes include the desire to make lucrative international sponsorship deals. To do so a company or brand needs to be globally established and understood to be used as a platform. (This was the main reason for Mars changing its UK-known Marathon chocolate and nut bar to the Snickers name by which it was marketed elsewhere.)

Not all image changes are wholesale, of course. Some would find cause for concern, too, in the expensive and seemingly pointless 'tinkering' that is reported of some big concerns. An oft-quoted example is BP's logo. Yet those in the image industry argue that the changes were necessary.

Mergers with US brands such as Arko and Amoco had put BP on the global stage, and the group needed to shift public awareness to take account of the fact that it was no longer simply an oil production company but a global energy brand, concerned with meeting world-wide energy requirements. BP's revised logo now denotes more of an energy-like 'flow'.

Measuring and managing intangibles

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The Faculty's half-day conference on 'Measuring and managing intangibles', chaired by Intellectual Capital Services director Tony Powell, provided suggestions for monitoring and reporting the performance of different elements within this particularly elusive class of assets. Helen Fearnley reports on the four principal contributions.

1 ValueReporting

David Phillips, a partner in PricewaterhouseCoopers and a founder member of the team which pioneered PwC's ValueReporting thinking and resultant conceptual model, argued the general case for reporting more of what investors and other stakeholders want to know – including a wide range of information that is not currently covered in standard financial reporting.

The ValueReporting team's research, said Phillips, found remarkable similarities in the information needs of markets around the world. They want to know about a company's financial and non-financial drivers, its intangible – as well as tangible – assets, and they want integrated reporting on risk and value. Their ideal is companies offering voluntary transparency – as opposed to simply complying with regulatory reporting requirements. And they want something more meaningful than just earnings and the game of creating and meeting earnings forecasts.

Phillips suggested that most companies stop short of the full value creation process. They create value, and manage it, but do not invest enough effort or money in value realisation – ie communicating their achievement to the outside world.

The evidence bears this out. The ValueReporting team's research showed that most CEOs feel their share price does not reflect the company's underlying value. Yet while these CEOs also consider themselves to be proactive in providing information, their investors' view is that the information offered is minimal.

In fact, Phillips observed, there are three different models for information provision – management accounting, financial reporting, and investment company analysis. Financial reporting, he added, is the key bridge but unfortunately falls well short of creating an effective channel.

As Phillips pointed out, "You can't report information you don't have; and you shouldn't be reporting information not used on a day-to-day basis." PwC has codified its research into the 'ValueReporting framework' initially in a generic form but also tailored for industries. This framework shows the main building blocks of value creation, and hence all the areas on which a company should be providing information (see box below).

> It is not enough to have a strategy... it must be conveyed to the market

The aim, he stressed, is the alignment of critical elements of information and, in particular, the better disclosure of intangibles. He also explained that this was not about valuing intangibles and putting them on the balance sheet, it was about analysing the inputs and output.

For example, it is not enough to have a strategy, it must be conveyed to the market along with specific goals. Similarly, concerning value creating activities, the management must be aware of its own value drivers – what provides its own competitive advantage.

Some companies are already moving towards such enlightened reporting. Those mentioned in Phillips' dispatches include Siemens (for its reporting on the different costs of capital for separate operating groups), DuPont (identifying the degree of innovation through percentage of revenues from new prod-

The ValueReporting framework

MARKET OVERVIEW >	STRATEGY >	VALUE CREATING ACTIVITIES >	FINANCIAL PERFORMANCE
• Competitive environment • Regulatory environment • Macro-economic environment	• Goals and objectives • Organisational design • Governance	• Customers • People • Innovation • Brands • Supply chain • Environmental, social and ethical	• Financial position • Risk profile • Economic performance • Segmental analysis

ucts introduced in the last five years), Heinz (brand information by country) and Systematic (detailed reporting on its people, and the trends in their working patterns and training).

Among the benefits of this sort of transparency, Phillips ventured, would be increased management credibility, more long term investors and higher share of access to new and lower cost capital.

2 Marketing

Dr Robert Shaw continued the intangibles theme with a review of the current state of measuring and managing value creation through marketing. Shaw is managing director of the Marketing Best Practice International (MBPI) consultancy and also visiting professor at Cranfield School of Management. In both roles he has been researching the progress of value creation by marketing – known as value based marketing (VBMk). This, he said, is not as well developed as value based management itself. Indeed, research both by the McKinsey consultancy and at Cranfield has shown that CEOs traditionally take a pretty dim view of their marketing departments' effectiveness in value creation.

Cranfield has designed a programme to establish how this might be improved, and to gather examples of existing marketing best practice. Based on this programme, Shaw went on to discuss the three key factors in VBMk – its calculation; the required toolset; and the management framework.

More than 50% of the market value of the average company now derives from intangibles. And finance directors surveyed believe the bulk of intangibles-generated value is driven by marketing, the brand, and customer relationships. Hence the need for measuring and managing these three is strong.

A premium brand, with its command of higher prices and better retail display, is a rich source of future revenues, which can be calculated fairly straightforwardly. By summing up the future cash flows from those leading brands, and doing an economic value added (EVA™*) or total shareholder return (TSR) calculation, you end up with a number for value creation.

However, choosing the appropriate toolset for marketing value creation is more of a challenge. As Shaw observed, there are hundreds of tools and techniques available (*see box, below left*). However, he added, most companies either underspend on these, do not know about them, or their finance directors refuse to use them for financial reporting purposes. There is no clear development path for these tools and techniques.

> One key use should be to highlight where value destruction occurs

One of the key uses of any of these tools, Shaw said, should be to highlight where value destruction occurs – eg in certain brands – so that capital investment can be cut off in those areas. He gave several examples where companies had successfully stemmed such value outflow. However, he added, in most companies the marketing layer of value creation measurement is "terrible". The current measures used – eg customer satisfaction – simply do not provide specific enough information.

On the matter of a management framework, Shaw admitted that marketing directors are not by nature good project people, and need to have a framework firmly imbedded. This should involve teamwork, setting priorities, and developing a knowledge of how the public reacts.

However, some companies are successfully getting to grips with measuring marketing value creation. Cadbury Schweppes is now applying the VBM initiated several years ago to its marketing function. In doing so it is looking at how it allocates its spend on specific brands (having already 'raised the bar' through announcing a goal of sustained double digit earnings increases). Most importantly, its CEO meets twice yearly with managers to discuss strategy and performance.

At IBM, an initially unsuccessful attempt to turn the group's marketing round began producing results when the CEO insisted his regular meeting with division heads be without their aides, ensuring that these managers were completely on top of the figures. At Diageo, management insists that everyone – including the company's investment analysts – be conversant with the means the group uses to measure and manage its brands.

Managements must, Shaw concluded, find out which parts of their marketing create value, and which destroy it.

Toolset

- Media optimisation
- Econometric models
- Advertising testing
- Brand dynamics models
- Activity based costing
- Balanced scorecards
- Brand equity monitor
- Pricing models
- Control risk self-assessment

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3 People management

Andrew Mayo, consultant, speaker and writer on international human resource management, spoke on the importance of measuring and managing human capital. He drew attention to the contrast between the lip service often paid to employees – eg 'they are this business's greatest asset' – and the tendency nevertheless to think of them as 'costs walking around on legs' or just 'headcount'. Business's unsolved problem, he went on, is: how to balance people's cost with a quantitative measure of their value.

An organisation needs a measure that takes account of the diversity of worth in people (even those doing the 'same' job). It requires a framework of people-

** EVA is a registered trademark of Stern Stewart & Co.*

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related measures which form an intrinsic part of an organisation's performance measurement system. It should quantify the financial and non-financial value added to each stakeholder through the people employed, ensuring that such value is increased, rather than decreased, as a result of merger or restructure. And, when the time comes that businesses are required to publish relevant, reliable information on intangibles, it must decide what to publish in the interest of investors and shareholders.

> People do not fit the financial definition of an asset

Some of the difficulties in achieving the above, Mayo said, include that people do not fit the financial definition of an asset, that performance measurement – being dominated by time-intensive management accounting – gives lower priority to other measures, and that HR people tend to react negatively to – and are not adept at – 'people measurement'. Also, with people measurement total objectivity is impossible, and value has to be judged in more than monetary terms.

Hence the quest cannot, perhaps, be to have an absolute measure of value added by human capital. But one should certainly be able to measure whether that value creation is getting better or worse.

Mayo summarised the ground covered since the 1970s in trying to find an approach to 'measuring' people – from Eric Flamholz's little-adopted human resource accounting formulae to the pioneering work in Scandinavia identifying the intellectual capital component as the difference between the market value and net book value of a company (*see box, top right*).

All these methods are in Mayo's estimate either somewhat inadequate or incomplete. Companies themselves, he added, tend to have 'bits and pieces' of people measurement systems, but without consistency – so there is no information on the trends. Yet many studies in the past six years have shown the relationship between good people management practices and 'bottom line success'.

Human capital valuation requires a different approach from that of standard accounting, and any chosen method will be used for internal comparisons, rather than external, Mayo said. Thus he suggested three areas to be measured: valuing people as assets; measuring their contribution to added value for all stakeholders; and monitoring the environment in which they work. The important factor, he said, being not absolute but relative performance (eg, is it enough? and is it increasing or decreasing?).

He introduced the concept of the 'human capital monitor', divided into three sections measuring, respectively, people as assets, their motivation and commitment, and their contribution to added value. He went on to describe the four key processes in maximising human asset value – their acquisition, retention, growth and exiting – and the drivers and indicators of success in this area, in particular the environment in which they contribute. Influential factors in that environment include leadership effectiveness, personal drive, the excitement of the work, and the physical conditions of the environment.

Existing approaches to 'measuring' people

- Human resource accounting (Flamholz)
- Relating "human resource practices" to bottom line results (Watson Wyatt, Huselid, ORC, Ulrich)
- Productivity and statistics (Saratoga)
- Return on investment (Kearns, Arthur Andersen)
- Efficiency of HR activities and processes (Ulrich)
- Balanced scorecard (Kaplan & Norton)
- Intellectual capital monitors (Sveiby, Edvinsson)

The challenge, in people measurement, is to link every individual or team to quantified value added. However, there is a danger in using too many measures. Ideally, there should be just a few enterprise-wide measures for benchmarking and reporting.

As Mayo concluded, "A value creating organisation will have more than a mere headcount budget – it will plan for the maximisation of its needed human capital and will monitor the plan with the same emphasis as its financial plans."

4 Reputation

Finally, Keith MacMillan, professor of business reputation at Henley Management College, explained the importance of reporting on stakeholder relationships as an indicator of future shareholder value and corporate reputation.

MacMillan argued that while corporate reputation may be an important intangible asset, or, indeed, liability, it is not an easy concept to pin down and manage.

This is because it is formed in people's minds and hinges on the perception of an organisation's character. In the case of a large multinational this may amount to millions of people, ranging from those who merely see a company's advertisements or press coverage to important customers, employees or suppliers.

Clearly, the views of this latter group are key, since the direct cash exchange between, say, a customer and the company can have a direct impact on shareholder value. Moreover, the better the relationship with these key stakeholders, the more likely they are to support the company and thus positively contribute to its performance.

Non-governmental organisations, competitors, analysts and others will also have views of the company – and may even take action against it – but crises can be averted when a company's key stakeholders remain loyal as a result of positive past experience. As the recent Enron, WorldCom and Arthur Andersen cases also dramatically illustrate, when crises in reputation do occur the effect can be dramatic, often resulting in the loss of an organisation's shareholder value and even bankruptcy.

For MacMillan, many current measures of reputation, such as press coverage or brand attributes, are inadequate because they fail to make the link with intended future stakeholder behaviours. Increased awareness of a company, or even measures of satisfaction, are similarly deficient. What counts, he argued, is future intended behaviour.

For unless companies know how key stakeholders will behave towards them in the future they do not have a handle on a crucial element in their intangible assets. Intended behaviours, he said, are likely to be based on stakeholders' current and past experience of the firm and will be driven by the feelings and attitudes that result from these experiences.

In the Henley Centre for Organisation Reputation and Relationships (CORR) model of stakeholder relationships and the associated measurement instruments (*see Figure 1, below*), stakeholder experiences and feelings are assessed and linked to future intended behaviours towards the company.

Moreover, MacMillan argued that companies should report on these aspects of their relationship with key stakeholders.

Not only, he said, do they represent the major part of the reputation of the business – a key intangible asset – but they can also be a guide to the general health of a business and its future source of shareholder value.

Summary

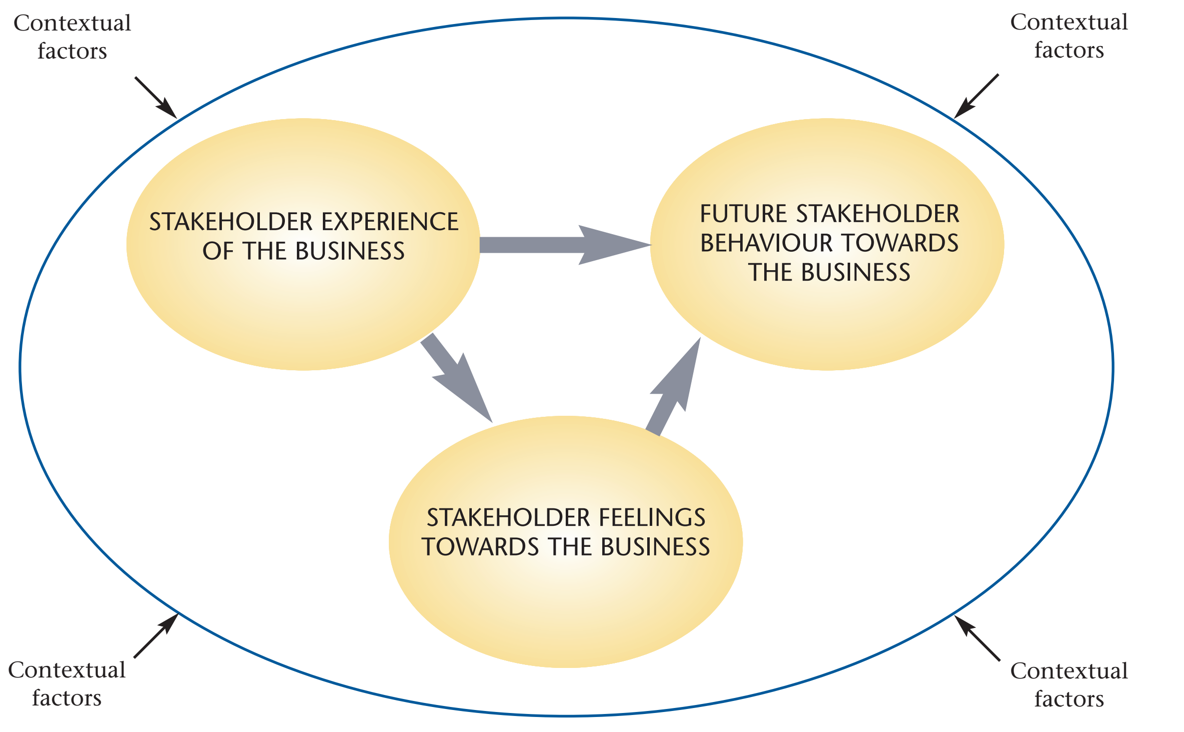
In conclusion, conference chairman Tony Powell pointed out how perceptions of the issue of measuring and managing intangibles have evolved.

When the importance of this subject was first recognised, he recalled, it gave rise to quite separate areas of research into measuring the value created by brands, intellectual property, patents, people and reputation. Nowadays there is some overlap between those areas.

He hoped the conference had provided increased insight into several aspects of intangible assets, and offered useful tools and techniques for their measurement and management. **F&M**

For useful web sites on reputation and other intangibles, see page 11.

Figure 1 **CORR model**



Value measurement and reporting – a new model

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Much has been made of the importance of businesses creating and reporting 'value'. Yet to date neither a standard definition nor a prescribed method of measuring and reporting it, has existed. Now, however, the accountancy profession worldwide is collaborating in an effort to establish just such parameters, as **F Anne Drozd** explains.

Much has been said and written about the need for new and additional reporting. The financial world is reeling with the impact of failures such as those of Enron and WorldCom. Investors are now saying, "We didn't know how bad things really were," "The financial statements didn't give us the kind of information we need!" and "The financial statements look backwards at historical data, not forwards to where the company is moving." These are the current cries of distress.

In addition, in the not-too-distant past, dotcom shares were trading at fantastic multiples of negligible earnings. The companies had no depth of historical data, no past records of successes or failures to point to, no trend information to talk about. As a result, investors, even knowledgeable ones, were shaking their heads over how to determine a realistic share price. Hence everyone started talking about 'value', but without a widely accepted definition of what value is.

A dictionary typically defines value as: 'the economic unit that a willing, knowledgeable seller and a willing knowledgeable buyer used to complete a transaction'; or 'the importance or significance of an object, idea, occurrence or process'.

The first definition is based on historical fact, while the second may be future-oriented, which can be difficult to quantify.

So, starting with the idea that value is more than just monetary worth, ways to measure and report the total value of a business, both its tangible assets and liabilities and its intangibles, are needed. But value reporting must be a collateral system to traditional financial reporting, not a replacement. A new reporting model is a bold step into the future; to tinker with the old reporting model and simply adjust it is not sufficient. The new reporting model cannot be incrementally developed. Backward-focused financial statements, based on realised value and delivered on a periodic basis, do not communicate value that can be created in the future and the risks and rewards of the business's operations.

> The accountancy profession has been the lead player in starting the collaborative

Some value reporting – but no comparability
Some companies have already started telling investors, financial analysts who study their companies, and others, about the value that their management and boards of directors perceive in their businesses. The examples presented in the PricewaterhouseCoopers' annual publications, 'ValueReporting', are drawn from companies in the financial services, technology and communications, and consumer goods industrial products and services sectors.

There are, however, no globally generally accepted standards (GGAS) for either measurement or reporting of this elusive concept of value. Consequently, there is no comparable basis for measuring and reporting value, as it pertains to a business, either as a whole or as a stand-alone economic unit within a larger entity. The absence of GGAS means that comparability between value reports is not determinable and that any independent review of value measurement must be done on an ad hoc basis.

The Value Measurement and Reporting Collaborative
To begin to fill this void, a group of interested and concerned bodies have formed the Value Measurement and Reporting Collaborative (VMRC or 'collaborative'). The purpose of the collaborative is to:

- bring consistency to needed changes in the reporting model and ensure the comparability of results when reporting;
- help develop, demonstrate and communicate best practices, market-driven principles and concepts that characterise value measurement;
- help gain general acceptance of those best practices, principles and concepts; and
- ultimately, work with all interested stakeholders to develop the new reporting model.

The accounting profession, represented by firms and institutes throughout the world, has been the lead player in starting the collaborative. It is hoped that, as quickly as possible, corporate directors, senior management of businesses, business associations and organisations, institutional investors, investment analysts, software companies, and academics will join VMRC.

It is also important that regulators are aware of the existence, objectives and efforts of VMRC, so that its efforts are complementary, and in sync, with those of other groups responding to regulators' requirements seeking to make incremental changes in existing reporting models. To allow regulators to maintain their independence, it is envisioned that they will not be members of VMRC.

VMRC does not see itself as a standard-setting body. The collaborative's goal is a framework of principles that will form guidelines. However, achievement of this goal will provide benefits for all stakeholders, and that is why companies will voluntarily want to be part of the formulation of the guidelines and adopt the reporting model.

Listed companies will experience better analysis by capital markets and a more stable stock price that reflects the future of the company's activities.

For investors, the benefits will include access to more – especially more forward-looking – information. Investors will also see standardised non-financial information and reporting among businesses, and the key drivers influencing a business's direction.

Value measurement and reporting does not benefit only listed entities. For example, non-listed public companies' boards of directors, as well as advisory boards of private companies and senior management of both will have better information for strategic decision-making and performance evaluation. Also, the dissemination of better, future-oriented information, particularly on a real-time and continuous basis, should result in access to lower cost capital for all entities.

Figure 1 **Value measurement definition**

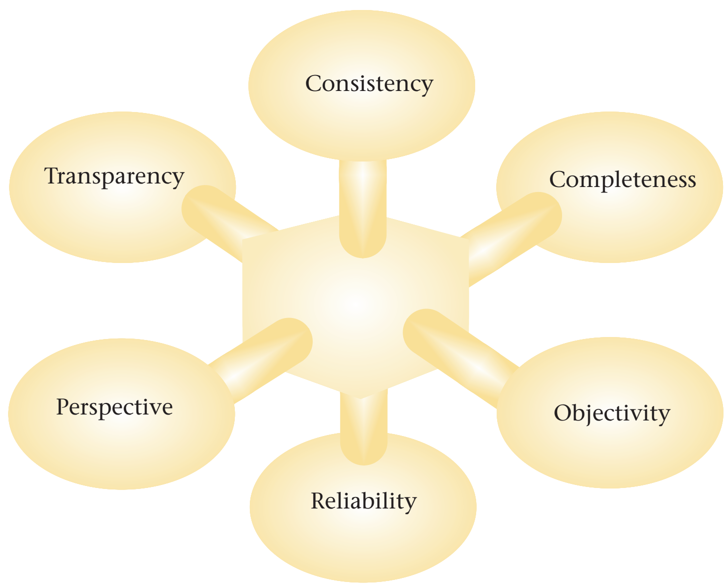
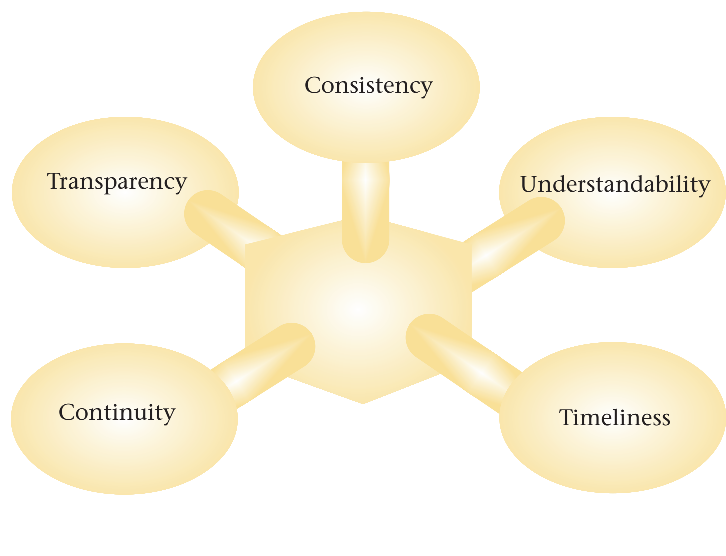


Figure 2 **Value reporting definition**



A first step

As its first step, the members of the collaborative have agreed on some preliminary definitions to be applied in the measurement and reporting of value. On the assumption that the ultimate standards will be principles-based, not rules-based, VMRC has adopted a definition of value measurement that comprises a framework of principles about perspective; transparency; consistency; completeness; objectivity; and reliability (see Figure 1, left). The definition of 'value reporting' includes transparency; consistency; understandability; continuity; and timeliness (*see Figure 2, left*).

To determine whether the measurement of the value of a business embodies these principles, there are some very basic questions that its board members or senior management can ask. They are:

- *perspective* – has value been calculated or described from many points of view, ie those of environmentalists or community activists, as well as those of the business's management and board and shareholders?
- *transparency* – are the assumptions, perceptions and events about what is perceived as valuable within the business (and what model or models, including key assumptions and drivers used, were employed in the estimation of value) clearly and easily apparent to the reader?

- *consistency* – have the same principles and procedures been employed from period to period in the same manner, until circumstances dictate a change is necessary? If there is a change in principles, procedures or assumptions, are the changes and the need for them transparent?
- *completeness* – does the estimation of the business's value include the consideration of financial and non-financial data about material or significant events, assets or processes that are relevant to value of the business? These include, for example, the business's market and its position in the value chain; a comparison of peers, competitors or related entities; and the business's key strategies for competing and key capabilities, in light of its mission, vision and goals?
- *objectivity* – is the report of the business's value capable of being reviewed by independent, objective, third parties or against acceptable benchmarks or measures? and
- *reliability* – could assurance be given on the report of the business's value by independent, objective, third parties?

In addition, to determine whether the value report is prepared in a manner that reflects the stated principles, a reader, should consider:

- *transparency* – has sufficient information been provided to enable the reader to make his or her own judgement of value?
- *consistency* – are the same principles and procedures employed in the preparation and presentation of information from period to period and by reporting businesses within a specific industry?
- *understandability* – is the information presented in a clear, expansive and unambiguous manner? Is the information given that cannot be reported in either standard economic or numerical units (eg, information about corporate governance or risk evaluation systems) comprehensible? Is information given in a financial or numerical format logically provided in that format? and
- *continuity and timeliness* – is current information provided regularly and consistently over successive periods?

There is a lot of work to be done. For example, at the present time, consistency of value reporting among reporting businesses in the same industry is not a principle that has been generally adopted.

Each business preparing a report on its value provides the information that its senior management believes is of significance to its operations without, necessarily, considering other companies in the same industry. The global financial community simply does not yet have generally acceptable benchmarks, let alone a widely accepted review process.

Hence VMRC is being launched. The contemplated research to be undertaken under the auspices of VMRC is very likely to require additions, deletions or revisions to the preliminary taxonomy of terms. In the meantime, VMRC is looking for comments and practical experimentation on such issues as:

- the identification of key components and value drivers;
- the relationships among value drivers; and
- methodologies for measuring value drivers. **F&M**

For more information about VMRC or to give your comments about its direction or planned projects, please contact either Anne at anne.drozd@cica.ca or Chris Jackson at chris.jackson@icaew.co.uk.

Useful web sites – intangibles

Corporate Reputation Institute: home page of the institute, which is based within Manchester Business School and works with organisations to understand how they manage reputation. The web site includes an explanation of the corporate reputation chain and a bibliography of their publications in this field.
www.mbs.ac.uk/corporate/cri/index.cfm

Corporate Reputation Review: leading international journal on reputation management published by Henry Stewart Publications which features best practice, surveys and articles on topical issues. The web site provides a taster of forthcoming topics and links through to a full table of contents listings for previous volumes.
www.henrystewart.com/journals/crr/

Reputation Institution: official web site of the private research organisation founded by Stern School of Business. The site includes a number of articles on reputation and links to a range of related resources on the internet.
www.reputationinstitute.com/sections/rep/rep.html

Valuing Intangibles: dedicated section of the Cap Gemini Ernst & Young Centre for Business Innovation web site on intangible assets, including the full text of issue 7 of the bi-annual journal 'Perspectives on business innovation' which takes 'Valuing intangibles' as its theme. The special issue includes six articles on intangible assets, with three articles focused on measuring and managing intangibles in the financial services, telecommunications and oil/gas industries.
www.cbi.cgey.com/research/current-work/valuing-intangibles/index.html

Intangible Assets Monitor: comprehensive information on the methodology of the Intangible Assets Monitor by Karl Erik Sveiby. The Intangible Assets Monitor is described on the site as a 'method for measuring intangible assets and a presentation format which displays a number of relevant indicators for measuring intangible assets in a simple fashion' and includes the option to click on indicators for more detailed information.
http://sveiby.konverge.com/articles/companymonitor.html

Intangibles – Measurement & Management: on-line bibliography of papers by Baruch Lev (director of the Vincent C Ross Institute of Accounting Research) on intangible assets with links to the full text where available. Includes the full text of 'Intangible assets: measurement, drivers, usefulness' by Feng Gu and Baruch Lev in Word format (32 pages, July 2001).
http://pages.stern.nyu.edu/~blev/intangibles.html

PROFILE

The desire to 'put something back'

Continuing our occasional series of Faculty profiles, Helen Fearnley talks to **Helen Jesson** (right), who was voted onto the committee earlier this year and who has experience in practice and industry.

Helen Jesson can be contacted by e-mail at spencom@btopenworld.com

Helen Jesson, the latest recruit to the Faculty committee, offered her services for the simple reason that she wanted to give something back. As she puts it, "After years of using the Institute's and, latterly, the Faculty's resources, I felt it was my turn to make a contribution."

During her time as a consumer of those resources, she says, what proved particularly valuable was the opportunity to 'connect' that membership of the Faculty afforded. This opportunity comes in two guises, she believes: "First, there is the chance to keep up to date with the information about the latest management ideas and theories – and to refresh one's memory of some of the longer-standing ones. In other words, one can connect with experts in various techniques and disciplines. Secondly, there is the chance to network among one's peers."

Jesson's career path since her 1984 degree in pure and applied mathematics has been varied.

Challenging

Her first nine years were spent with KPMG, in both London and Australia. The latter she particularly relished, both for the hard-working and fun-loving nature of the Australian people, and the excitement of working in a different culture. However, her time there was also extremely challenging, involving – inter alia – managing the internal audit of the pension fund for all state employees (firemen, teachers, etc) of Victoria. The fund, which had weekly outgoings of A$20 million, and total liabilities of A$15 billion, had a new management team who were striving for a change in culture and internal audit was part of that process.

In the UK, her KPMG work – always more weighted towards one-off projects than routine audit work – included working on BAe's disposal of Rover, and on the flotation of Carpetright, as well as managing the audit of EDS.

Once the recession of the early 1990s was over, Jesson made the move which had long been her intention – to work in industry. She joined Ladbroke's Hotels and Casinos, now Hilton Group, in March 1995.

> 'I felt it was my turn to make a contribution'

There, as senior financial analyst, she was responsible for the group reporting of results for the Hilton hotels and casino divisions, plus consolidating the budget and forecast reporting for the whole group and preparing the relevant board reports.

While there, she designed and implemented a group wide monthly cash flow and balance sheet reporting system, and introduced a formal forecasting process three times a year.

Eighteen months later came the move to United Biscuits (UB). Jesson first joined as a financial planning and analysis manager for Western Europe, but just over a year later was invited by the managing director of Western Europe to join his team as head of business development in Western Europe.

Not long after that, UB made a significant acquisition which included a substantial Belgian business. Jesson was made finance director of UB Belgium, and was immediately immersed in the enormous task of integrating the new acquisition – particularly the systems – with the rest of the group.

Decentralised

During this period Jesson created a stand-alone country unit from the previously centrally controlled pan-European organisation, and implemented both a new transaction system (JD Edwards) and a data warehouse (Powerplay) – as the latter did not exist previously and the former was not millennium compliant.

She also designed a finance function for the acquired company to match the new decentralised structure, recruited the team to run it, instituted a detailed reporting process that also complied with group reporting requirements, and delivered on every budget and forecast despite the pressures of the integration.

Additionally, she implemented UB's new matrix management structure in the Belgian unit; and advised the board for or against various continental transactions after conducting financial and strategic analysis.

The particularly challenging circumstances of her years in industry have convinced Jesson of the importance of the Faculty as both a source of information on latest management trends, and as a sounding board.

Ultimately, Jesson hopes to be party to continuing the Faculty's tradition of providing a forum for the pooling of ideas and experiences, as well as disseminating information on all the latest management theories and techniques. **F&M**

MARKETING

To rename, or not to rename...

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

Complementing our article on the rationale of the corporate name change on page 1, **Alan Mitchell** uses his latest Marketing Update to outline when it is (or, frequently, is not) a good idea.

Words are mere empty shells into which we pour socially constructed meaning. Sorry for such an off-putting piece of philosophy but it's useful when it comes to the controversial arena of brand (and corporate) naming.

Given time and experience, any word can come to mean anything. There's no reason, for example, why Ford should stand for cars or Sainsbury for groceries, but we've grown used to the idea. Likewise, we don't bat an eyelid when someone uses the word Virgin for an airline, Apple for a computer or Orange for a phone service. Over time, we've simply filled an empty vessel with new meaning.

So why has naming become such a hot issue? In earlier, simpler times naming was easy. Most companies simply took the name of their founder: Cadbury, Ford, Gillette, Heinz, Kellogg, Marks & Spencer, Michelin, Procter & Gamble, Sainsbury, Unilever, W H Smith, Wal-Mart (from founder Sam Walton), etc. It's hard to think of an accountancy firm, law firm or management consultancy that hasn't followed this route.

Others simply described what they did: International Business Machines, British Petroleum, Imperial Chemical Industries, Minnesota Mining and Manufacturing, Microsoft (software for micro-computers).

A few conjured names out of thin air, like Sony and Vaseline. Kodak founder George Eastman anticipated many a modern debate when he explained: "I knew a trade name had to be short, vigorous and incapable of being misspelled to an extent that would destroy its identity, and, in order to satisfy trademark laws it must mean nothing. The letter K had been a favourite with me – it seems a strong, incisive sort of letter. Therefore, the word I wanted had to start with a K."

But Eastman had it easy. He was starting out with a blank sheet of paper. Today's big challenge isn't so much in naming, but in re-naming; not in filling an empty vessel but emptying full vessels – names which have come to mean things we no longer want them to mean – and refilling them with some new content. That's a much harder task.

> Change your company's name as often as you change your own

A number of strategies have evolved. One is to collapse old names into strings of meaningless letters: from International Business Machines to IBM, Imperial Chemical Industries to ICI, Bayerische Motoren Werke to BMW, Australian Mutual Provident to AMP, and so on. One drawback: it's not easy to build a brand out of an acronym. IBM, the BBC and 3M may have achieved it. But most are just beginning.

Another route – traditionally favoured by professional firms – is to reflect the name of a new 'senior' partner. One merger creates Smith Kline Beecham, then we get Glaxo Smith Kline, and so on. Drawback (notwithstanding politics and egos): each new twist in the corporate tale demands yet another re-naming exercise.

A third approach has been to follow the Kodak route and invent new, meaningless words: Avensis, Corus, Diageo, Vivendi. The trouble here: obliterating the past does nothing to build for the future. It creates a vacuum, not new meaning.

The critical issue for all three approaches (including those who dream of calling a management consultancy 'Monday' or 'BearingPoint') is that meaning takes time to build: consistent repetition, ongoing usage, endlessly reinforced experience. And there's no short-cut for time.

So what should we do? Naming consultants, who have arguably puffed up their roles (and their fees) by pretending that naming is both more important and more difficult than it is, have a vested interest in promoting name changes. The press, smelling a rat, are now minded to ridicule every such attempt.

Here's a suggestion. First, the basic rule should be: change your company's name as often you change your own. What matters is consistent, painstaking explanation and communication.

People's perceptions change with experience, so evolutionary experience is usually far better than revolutionary naming. Swedish company Stora has moved from copper mining through hydro power to paper, wood pulp and chemicals without ever changing its name.

Rule number two: if you really, really have to change your name (as many women accept on marriage) do so decisively and for the duration.

Rule number three (the clincher): if you have to keep on changing your name, then almost certainly the problem doesn't lie with the name. It lies with your business. **F&M**

FINANCIAL REPORTING

Get financial instruments right, said FRED 30

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.

Here **David Chopping** looks at the changes which are being suggested in the area of financial instruments reporting; and why it is not too soon to start taking these intentions into account.

Sometimes it is tempting to ignore exposure drafts. Accountants have quite enough to deal with making sure they are up to date with things that are in force, without worrying about things that don't even apply yet. Tempting, but dangerous.

The last of the recent group of exposure drafts from the Accounting Standards Board (ASB) is the massive Financial Reporting Exposure Draft (FRED) 30 – 'Financial Instruments: disclosure and presentation, recognition and measurement'. Although its title is slightly misleading – given that the actual proposals do not deal with recognition, pending changes in the equivalent international standard – this is not a draft that should be ignored.

Some of the changes associated with the move to international standards have been covered in a previous article. Now we have what are, in effect, the transitional provisions for financial instruments prior to the change in 2005.

The draft proposes that the new rules apply from 2004, and only its presentation rules will apply to all companies, other than very small ones. Of the rest, the disclosure rules will apply purely to listed companies and banks and are very similar to FRS 13. The measurement rules will be optional, applying only to companies that choose to adopt a fair value accounting model.

Distinguishing liabilities and equity

The changes of widest application are therefore those associated with presentation. Within that category, the first major change affects the distinction between liabilities and equity. Under current UK rules, primarily FRS 4, anything that is legally a share is accounted for as a share. Shareholders' funds are split between equity and non-equity, but they remain shareholders' funds. FRED 30 proposes that a substance over form approach be taken.

If an item contains an obligation to deliver cash, or financial assets, then it is a liability. This means that some preference shares will become liabilities under FRED 30, equivalent to other forms of debt. This will apply where there is a fixed or determinable redemption date, or where the holder has the right to call for redemption. Of course, if an item is debt, then, logically, payments on it must be interest.

> Although its title is misleading, this is not a draft that should be ignored

This is exactly the inference made by FRED 30. Where dividends are paid on such preference shares then these will be shown as interest. (Separate disclosure from other types of interest is encouraged, to reflect the different legal status of the instrument.)

FRED 30 also addresses compound instruments. Compound instruments are those that contain both a liability and an equity instrument. The simplest example is probably convertible debt. The current guidance on convertible debt is simple: it should be treated as debt unless and until it is converted. The only current implications are for disclosure. Under FRED 30, this will not be the case. Convertible debt must be broken down into its two parts: a debt, and a conversion right. As a general rule, companies issuing convertible debt will have a lower interest rate than they would on standard debt. (If this were not the case, what would be the point in giving the conversion rights?)

Given that the cash flows are fixed, the debt element is therefore the present value of the cash flows, discounted at the rate that would have applied if the conversion rights had not been granted. This will be less than the amount received. The difference is therefore the value of the conversion rights. This difference is taken directly to equity, as it is not a liability.

The new proposed treatment was considered at the time FRS 4 was drafted. It was rejected as unnecessarily complex. As it cannot have become any easier or harder in the intervening years, it must be the definition of what is considered necessary that has changed.

Why the urgency?

So why is a standard expected in 2004 relevant now? There are no current transitional provisions, nor are they likely. It would not make much sense for, say, two types of preference share to be shown in different places in the accounts according to when they were issued. Some of the items that will be affected by the proposals are in issue now.

And of course current financial statements need comparatives, and comparatives need opening balances. Three years of numbers, when 2004 is only two years away. **F&M**

FORTHCOMING FACULTY EVENTS

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 Kirsten Fairhurst 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 Kirsten Fairhurst on 020 7920 8486.

● **7 November**
EVENING LECTURE (Chartered Accountants' Hall, London)

'LEADERSHIP UNPLUGGED – A NEW ROLE FOR THE FINANCE DIRECTOR' – STEVEN SONSINO, LONDON BUSINESS SCHOOL

How can finance directors, who are usually the most knowledgeable individuals, become more persuasive and even more influential within an organisation? Steven Sonsino, a fellow of the Centre for Management Development at London Business School, provides some ideas. Registration is at 5.45pm; the lecture is at 6.00pm; the buffet and networking start at 7.00pm.

● **3 December**
EVENING LECTURE (Chartered Accountants' Hall, London)

'REALITY CHECK – THE KEY ROLE OF STRATEGY IN CREATING WEALTH' – BOB GORZYNSKI, BRISTOL UNIVERSITY

After the collapse of several 'new economy' companies, this lecture looks at what went wrong and also examines the key role of strategy in creating long-term wealth in today's rapidly changing markets. Bob Gorzynski of Bristol University also discusses the role of financial professionals. Registration is at 5.45pm; the lecture is at 6.00pm; the buffet and networking start at 7.00pm.

2003

● **22 January**
EVENING LECTURE (Chartered Accountants' Hall, London)

'LINKING VALUE WITH VALUES – THE BEHAVIOURAL ASPECTS OF FINANCE' – MALCOLM LEWIS, STRATEGIC VALUE PARTNERS

With people and organisations moving ever faster, Malcolm Lewis of Strategic Value Partners will discuss 'hard' and 'soft' organisatonal issues, showing that linking value with values is the key to creating long-term success. Registration is at 5.45pm; the lecture is at 6.00pm; the buffet and networking start at 7.00pm.

RECORDINGS OF FACULTY LECTURES

The following lectures and conferences held by the Faculty in 2002 are available, in both **audio** and **video** format.

To obtain a recording, please tick the audio and/or video box on the tear-off response form opposite.

There is a charge of £5.00 for audio recordings and £10.00 for video.

18 FEB VALUEREPORTING – A REVOLUTION?
David Phillips of PricewaterhouseCoopers explains this new technique including how to manage for value and the benefits of greater transparency.

15 APR STRATEGIC ENTERPRISE MANAGEMENT
Martin Fahy of the National University of Ireland, Galway, discusses strategic management accounting decisions aimed at increasing shareholder value.

28 MAY PAY FOR PERFORMANCE – DIRECTORS' REMUNERATION
Ruth Bender of Cranfield School of Management discusses the structure of directors' remuneration in the context of creating value for shareholders.

18 SEP HUMAN CAPITAL – MEASURING PEOPLE AS ASSETS
Andrew Mayo, a consultant on international human resource management, discusses how to balance people's cost with a quantitative measure of their value.

Scottish members look 'beyond budgeting'

At a meeting of the newly-formed Institute Members in Scotland group, **Jeremy Hope** of CAM-I's Beyond Budgeting Round Table (BBRT) explored the shortcomings of the traditional budgeting model, and the ways in which some companies are now adopting approaches more appropriate to the current business climate.

Jeremy Hope is a programme director at CAM-I's Beyond Budgeting Round Table
E-mail: jeremyhope@onetel.net.uk

Approximately 30 members of the Institute's recently formed 'Institute Members in Scotland' (IMS) group met in Stirling in September for a presentation by Jeremy Hope of CAM-I's Beyond Budgeting Round Table (BBRT). The presentation was arranged by the IMS group in collaboration with the Faculty of Finance and Management for the benefit of Institute members in Scotland.

As regular readers of Faculty publications will be aware, the BBRT has been at the leading edge of research into emerging approaches to budgeting and other aspects of performance measurement and monitoring. Hope's wide-ranging presentation highlighted the financial, strategic and cultural problems of the traditional approaches to budgeting and target setting and explained why these disadvantages have become increasingly apparent in recent years. He then examined the evidence from organisations that have moved away from traditional approaches and outlined the emerging 'core principles' that the BBRT has identified from a study of these cases.

Having briefly explained how existing financial management concepts – such as activity based costing, the balanced scorecard and shareholder value models – could complement the 'beyond budgeting' model Hope outlined some of the key implementation challenges organisations would have to address if they wanted to revise their approach to strategic business performance measurement and management.

After the formal presentation attendees were able to discuss the issues raised both with Hope and among themselves over a buffet lunch and some lively discussions ensued. This was the first in what it is hoped will be a series of events reflecting the work of both the Faculty and the IMS. **F&M**

If you would like more information on the Faculty's activities in Scotland please contact John Fanning on 0131 2296915. If you want to know more about the IMS please contact Fiona Ormiston on 01383 882645.

IN DECEMBER'S MAILING...

Finance & Management, Issue 94
- 'FRS17 – a major worry for SMEs', by John Tranter, finance director of Eaton-Williams.
- 'Maximising the offer', by Dr Eddie Obeng, founder of Pentacle, the virtual business school.
- A report on the recent Faculty lecture 'Enterprise planning systems – do they measure up?', given by business software analyst Dennis Keeling.

Good Practice Guideline, Issue 40
- 'Real options techniques in capital investment' – an in-depth look at the issues involved in real options, written by Alison Hennell and Alison Stiles, who design and deliver financial learning programmes for people in business. This *GPG* focuses on the valuation of these various options and how this information can be used to make better investment decisions.

Finance & Management

... is edited and produced on behalf of the Faculty by Silverdart Ltd, Unit 211, Linton House, 164-180 Union Street, London SE1 0LH. Tel: 020 7928 7770; fax: 020 7928 7780; contact: Alex Murray, Gabrielle Liggett or Helen Fearnley.

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