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By Stephen Barlas, Dallon Christensen

GOVERNMENT

Cross-Border Swaps Proposals Worry Business Groups

By Stephen Barlas

The Dodd-Frank Act swaps rulemaking just keeps on giving. Previous columns have covered the proposed rules from the Securities & Exchange Commission (SEC) and U.S. Commodity Futures Trading Commission (CFTC) on margin requirements for end-users, defined as nonfinancial companies who use derivatives to hedge business risks (at least how the agencies see it). One of the big issues that has emerged in a number of SEC/CFTC Dodd-Frank derivatives rulemakings is whether the centralized treasuries at nonfinancial companies should be considered financial and, therefore, subject to margin. The latest set of SEC/CFTC proposed rules underlining that issue are those on cross-border swaps, which are when a company in the United States enters into a deal with a counterparty overseas or when a U.S. subsidiary overseas works with a U.S. swaps dealer.

At a macro level, the issue is whether the SEC and CFTC should allow a transaction between a U.S. and a European company, for example, to be regulated by the European Union. This has become known as "substituted compliance." Hal Scott, director of the Committee on Capital Markets Regulation, says the CFTC and SEC proposals "do not allow for sufficient deference to the laws of foreign jurisdictions with comparable swaps rules." He adds, "Essentially, the SEC has allowed for a broader substituted compliance regime, with more cross-border security-based swaps eligible for substituted compliance than is true for swaps falling under the CFTC's jurisdiction."

The big issue here for U.S. end-users, which primarily include industrial companies and manufacturers, is whether a foreign affiliate is defined as a "conduit affiliate." The CFTC subjects conduit affiliates to regulation, whereas the SEC doesn't, at least not yet. The Coalition for Derivatives End-Users, which represents the National Association of Manufacturers (NAM) and other business trade groups, believes the conduit concept should be rejected or, at a minimum, should exclude end-users and not be applied to security-based swaps in which neither party is a security-based swap dealer or major security-based swap participant. The Coalition is concerned that non-U.S. centralized treasury units could be categorized as conduit affiliates and therefore could be disadvantaged when transacting with non-U.S. counterparties.

Congress Urged to Force SEC's Hand on Proxy Advisor Regulation

Business groups are trying to clip the wings of proxy advisors who have been successful at convincing institutional shareholders to demand restrictions on corporate pay. The SEC published a concept release on the U.S. proxy system in July 2010 but hasn't taken a second step. In its report for fiscal year 2012, the SEC said it would be developing interpretative guidance on conflicts of interest in fiscal 2013. But that hasn't happened yet either. The U.S. government's fiscal year 2013 ended on September 30.

The Chamber of Commerce, Society of Corporate Secretaries and Governance Professionals, and Center on Executive Compensation are among those asking Congress to force the SEC to move forward with new rules limiting perceived conflicts of interest at firms such as Institutional Shareholder Services (ISS) and Glass, Lewis & Co. Those two are the dominant proxy advisory firms and have been successful in persuading shareholders to vote against a relatively small number of pay packages during the "Say on Pay" votes companies have been conducting for the past three years. Those votes were

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established by the Dodd-Frank Act. Shareholders vote for or against pay packages for the CEO and four other top-paid executives. The vote is voluntary, meaning the company can ignore it or change the pay package according to votes. ISS and Glass Lewis have been recommending what critics refer to as "homogenized" compensation, which includes a relative total shareholder return (TSR) metric in its computation for the long-term incentive for their CEOs.

Harvey Pitt, founder and CEO of the global business consulting firm Kalorama Partners and a former SEC chairman, says, "ISS operates a consulting division that provides advice to the same public companies about which ISS opines and influences institutional votes." He continues, "Glass Lewis is owned by an activist institutional investor—the Ontario Teachers' Pension Plan—and yet Glass Lewis takes positions on the precise issues its parent company forcefully advocates for public U.S. companies."

Even some leaders in the institutional investment community favor SEC action. Lynn Turner, a former SEC chief accountant and director of research at Glass Lewis and now the managing director at the economic and forensic consulting firm LitiNomics, believes "proxy advisory services should be subject to SEC oversight."

FASAC Releases 2013 FASB Stakeholder Survey Results

The Financial Accounting Standards Advisory Council (FASAC) released the results of its 2013 survey of stakeholders' views on the future agenda of the Financial Accounting Standards Board (FASB). The primary advisory group for the FASB, the FASAC strives to advise the Board about its future priorities, projects, and any new or potential agenda items.

Survey respondents included FASAC members as well as members of other FASB advisory groups, FASB Board members, and other external stakeholders. The results provide a glimpse into the stakeholder views about which items and issues should be on the FASB's future agenda, particularly for the next three to five years. Key observations include the top five projects that should be on the Board's agenda; the need to complete some of the potential projects in the next 24 months, as well as input on which projects; and the importance of completing key projects currently on the agenda.

Respondents indicated these priorities were important because of a greater need for simplification and better information. They felt that the current information available isn't useful in helping investors and other financial report users make decisions. FASAC Chairman Charles Noski said, "While opinions varied on specific projects and issues, FASB stakeholders agreed that simplifying standards, and improving the relevance of information that results from those standards, should be among the Board's top priorities." In addition, about half the respondents also support reorganization or enhancement of the FASB's *Accounting Standards Codification®*.

The top projects that respondents felt should be on the FASB's agenda in the next three to five years were:

1. Disclosure Framework,
2. Accounting for Financial Instruments: Hedging,
3. Conceptual Framework,
4. Financial Instruments with Characteristics of Equity,
5. Pensions (tie), and
5. Financial Statement Presentation (tie).

The complete results of the FASAC survey are available for download on the FASB website (www.fasb.org).

Sharing Your IMA Life

Most IMA® members share a strong spirit of camaraderie. What have your experiences as a member of IMA been like? Do you have a story about them you'd like to share? If so, please consider writing an IMA Life column that will be published in *Strategic Finance*. You can be a student member, a young professional, in the midst of your career, or retired. If you would like to write an IMA Life article, please e-mail Kathy Williams at kwilliams@imanet.org.

BOOKS

Managing Change

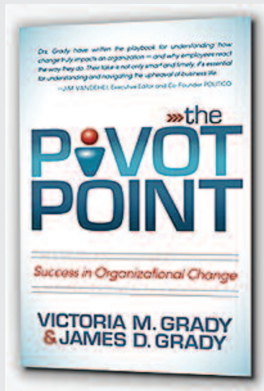
Change in organizations can be frustrating, difficult, and painful. It's also necessary. As financial leaders, we must balance the human element of change with analytical requirements. *The Pivot Point: Success in Organizational Change*, by the father-daughter team James and Victoria Grady, gives financial leaders a parable-based look at how people respond to change.

The book's introduction immediately details a telling statistic: 68% of organizational change initiatives fail. That sobering statistic leads to several factors that affect employees who are part of change efforts:

- Change is out of their control.
- Employees are pressured to change without feeling valued.
- Employees can feel distrust toward the organization.
- Employees feel like they're only resources or tools to make the change happen.

Unlike most organizational leadership books, *The Pivot Point* was written as a parable that focuses on six people stuck at a Washington, D.C., hotel conference as a hurricane passes through:

- Dr. Bankston, a university professor and author who was scheduled to speak at the conference before the hurricane canceled it;
- Jake, an IT director for a government agency;
- Liz, a medical director at a hospital;
- Joan, a rising star in a small business;
- Edward, a young project manager; and
- Hilde, a German operations executive in a business where the owner may retire soon.



The group members represent the different challenges and fears people experience during major organizational change efforts. The individuals face their own fears and uncertainties within their own organizations. Even if you haven't faced these specific situations, they're undoubtedly familiar. *The Pivot Point* is such a good read on change management because you can put yourself in the characters' shoes and ask how you would handle your own situation and why.

After getting stuck at the hotel during the storm, Bankston leads his five participants through a variety of readings and interpretations to identify the key factor that impacts change projects: attachment. This insight really struck me because I've been part of several software implementations and other business transformation projects during my career. The logic of these change projects seemed reasonable, but much of the resistance from employees occurred because of their attachment to the way things were done in the organization. The five "students" in the book discuss how their organizations are attached to key artifacts, processes, or other operations. Reading it, it's likely you'll apply this to past experiences, which is the strong point of a parable instead of a traditional, research-based book.

At the end of the parable, the authors present their research. Their centerpiece is the Loss of Organizational Effectiveness (LOE) index, which combines the business and human factors of change and quantifies the impact on an organization. They link individual factors to the symptoms of organizational problems. I found the index to be easy to understand and something I can use in my role as a finance director/CFO as my organization undertakes several significant change projects.

The Pivot Point is a quick read, spanning about 100 pages, but don't mistake brevity for depth of content. This parable was one of the most understandable and applicable books on change management I've read. I'm planning to have the rest of my senior management team read and discuss this book, and other organizations should do the same.

—Dallon Christensen CMA, CFM, CGMA, CPA/CITP, dc@dallonc.com

To listen to a podcast from author Victoria Grady, visit www.whiteboardbusiness.com/034.