

# Reporting to the board

## INTRODUCTION

The key purpose of treasury reports to the board is to enable directors to understand the exposure to financial risks, the effectiveness of risk management and the likely impact on the company's financial performance.

While there are no universally applicable standards for the form and content of treasury reports to the board, a set of common issues can be identified. The manner and extent of reporting will depend on the size of the company, its organisational structure, the nature of its operations and the size and type of financial risks to be managed. Board reports should reflect policy requirements, risk appetite, available resources and operating structure.

## Scope and content of reports

In all companies, reports should be broken down by type of risk and management activity. They should address accountability and identify actual performance against relevant benchmarks and policy guidelines. The main items relating to financial risks include:

- liquidity and funding position;
- interest rate exposure;
- currency exposure;
- commodity prices;
- credit/counter-party;
- financial structure;
- market conditions;
- compliance with approved policies and procedures; and
- effect of treasury transactions on the company's financial performance.

Reports should include a description of conditions in the financial markets over the period, make comparisons with previous periods and highlight any potential influence on the organisation's performance that may require adjustments to policy. For each exposure identified and measurable, the report should include:

- current level and nature of hedged and unhedged exposures; and
- sensitivity analysis which shows the effect on underlying risk of movements in interest rates. This could be done as an assessment of the effect of prospective movements on profit and loss, or on a mark-to-market basis.

Information relating to specific risk categories that might be included in the treasury report is detailed below. Not all of the matters in this outline will apply to all organisations. In some cases, additional information might be necessary; in others, a number of the points might be combined. The list is not exhaustive.

## Liquidity and funding risk reporting

This could include:

- actual, budgeted and historical cash flows, monthly cash flow projections for the next 12 months and quarterly projections for the next year;
- details of the utilisation of committed (and uncommitted if appropriate) funding lines by maturity and source, and unused committed funding lines by maturity and source;
- the funding plan for projected future requirements by maturity and source;
- volumes of securities on issue, recent new issues and secondary market turnover, relative to policy targets;
- a comparison of issue margins with comparably rated issuers; and
- actual, budgeted and historical volumes on issue, new issues and turnover, and projections for the following year.

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## Interest rate risk reporting

Interest rate risk reporting could include:

- the weighted average interest rate and term structure of the organisation's liabilities before and after the effect of any hedging transactions and, if appropriate, the match with the assets they support or the risk-neutral profile established by policy. For ease of reference, this schedule might also set out the policy specifications for interest rate and term-matching purposes together with comparative data (e.g. the position at the same time in the previous year), budgets and projections;
- a summary of transactions or instrument categories in defined terms and the nature of any open or unhedged positions;
- a comparison of the organisation's weighted average interest rates with equivalent actual market rates; and
- a performance comparison of actual debt cost relative to the risk-neutral benchmark.

## Foreign exchange risk reporting

Foreign exchange risk reporting could include:

- current and projected foreign exchange exposures, without taking into account hedging transactions or positions, by currency and type (e.g. translation);
- net foreign exchange exposure after hedging cover or offsets from natural positions (subject to accounting and taxation clearance) and financial market transactions. This should include a comparison with board policy on foreign exchange risk;
- a summary of foreign exchange hedging activity, by transaction type;
- budgeted and actual historical and current exchange rates relevant to the organisation's operations; and
- "What-if" scenarios to help directors understand the implications of the organisation's position.

## Commodity price risk reporting

Commodity price risk reporting could include:

- current and projected commodity price exposures by type before taking any hedging transactions into account;
- net commodity price exposure positions after hedging cover or offsets, compared with board policy requirements;
- a summary of commodity price hedging activity;
- budgeted and actual historical and current commodity prices relevant to the organisation's operations; and
- stress testing of commodity prices on the organisation's financial position.

## Credit risk reporting

Credit risk reporting could include:

- peak settlement or delivery exposures against approved limits, and
- any outstanding transactions in excess of policy limits and any counter-party defaults, with an explanation of the current status.

## Financial structure reporting

Financial structure reporting could include:

- current balances of issued capital, capital reserves, revenue reserves, subordinated debt, current borrowings, long-term borrowings and unused committed facilities and forecast movements;
- costs incurred in servicing the above financial structure including dividends and interest;
- financial structure ratios and percentages which measure the status and condition of the financial gearing, interest cover and debt maturity, for example, capital gearing, interest cover, cost of capital, stand-by credit and debt maturity profile; and
- mandated rates under borrowing covenants.

## Market conditions reporting

Market conditions reporting could include:

- a description highlighting financial market conditions which may effect the organisation's performance and influence future strategy; and
- stress testing of the firm's total financial position in extreme situations (3 to 7 standard deviations in the market).

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## Compliance reporting

Compliance reporting could include:

- certification that all policies have been adhered to;
- instances where stated policies have been breached;
- reasons for the breaches and what actions, if any, have been taken to rectify the situations;
- a summary of deals outstanding or unconfirmed or that are in excess of total limits; and
- investigations into failed settlements or limit breaches.

## Financial results of treasury transactions

Financial results could include:

- realised gains and losses for each risk area based on figures supplied from the general ledger by staff independent of treasury dealers;
- unrealised gains and losses on all forward and off-balance-sheet transactions identified for each risk area. Wherever possible, the result should be based on independent valuations made by accounting staff independent of treasury dealers and reflect:
  - independence of data (prices, rates, etc);
  - consistency of data (same source); and
  - the integrity and accuracy of the valuation models.

## Soft issues

These could include;

- staff changes, vacant positions;
- educational issues for directors on new products.

## FORMAT AND FEATURES OF REPORTS

Because of the importance of treasury activities, reports to the board should be presented in a form that delivers clear, concise and helpful information. The detail must be sufficient to satisfy directors that they are properly informed of relevant facts.

The following features will enhance the effectiveness of board reports:

- *brevity* – key issues should be summarised so that the attention of the board can be focused on principles rather than minor detail;
- *forward perspective* – effective management requires a focus on the future. This includes ‘testing’ portfolios in simulations of changed market conditions;
- *illustration* – reports can be supported and enhanced by visual and verbal presentations. Graphical techniques and projections can explain, emphasise and highlight issues and aspects of performance. Icons and colour can also help to get a clear message across;
- *key changes* – reports should highlight changes from previous periods, including changes in underlying exposure and hedge positions;
- *integrity* – reliability and accuracy of information;
- *clarity* – key information should be clear and understandable and be relevant to the organisation; and
- *timely circulation* – written reports should be distributed to the board before the meeting to ensure that directors have time to evaluate the information and define issues that need clarification or further details.

In general avoid the use of maths and calculations.

## FREQUENCY OF BOARD REPORTING

Typically, a board would have monthly meetings, although small or medium-sized companies with only executive directors may find that quarterly formal meetings are adequate.

The frequency of treasury reporting will depend on the nature of the information required, including the magnitude of risks. In normal circumstances, results of transactions and assessment of risk exposures will be reported to the monthly or other meeting at which financial results are reviewed. More frequent reports may be required if significant occurrences could affect financial results. The following are typical requirements for the frequency of reports to the board:

- *daily* — reports of any significant effect on the business arising from movements in market rates as they occur or substantial fluctuations in the value of completed transactions;
- *monthly* — profit or loss calculations, market conditions, performance against benchmarks, sensitivity and compliance;
- *quarterly* — policy review in light of financial markets or other external influences; and
- *annually* — review of policies, suitability of treasury objectives and risk parameters, funding plan and treasury performance as part of the planning cycle.

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# Reporting to the board

## HOW DO YOU GET CONFIDENCE IN THE REPORTS?

Board reports should present a complete, accurate analysis of key aspects of each issue. They should be capable of verification.

Depending on the size and nature of the company, the finance director or other senior finance executive will be responsible for the quality of treasury reports. Internal audit will provide periodic independent verification by substantive and compliance testing in line with the audit program.

External auditors may also be asked to conduct a special review of reports as part of an annual verification process, particularly in respect of financial instruments and derivatives.