



CAPIX Software IAS39 Compliance

Overview

Ready or not, the new International Accounting Standards will take effect from the first full accounting period from 1st January 2005.

CAPIX is actively committed to ensuring that our software products comply with the new International Accounting Standards (IAS). In particular, there are two IAS which are of special relevance to treasury operations:

- **IAS 32** - Financial Instruments: Disclosure and Presentation
- **IAS 39** - Financial Instruments: Recognition and Measurement

For many corporate treasuries this will not only mean changes to their hedge accounting procedures and policies, but the way they manage risk. The compliance impact of IAS 39 on corporate treasuries can be compared with the "Year 2000" preparations of the computer sector in 1999.

Capix Software and IAS Compliance



International
Accounting Standards
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CAPIX is committed to ensuring that its software packages keep abreast of current user requirements. This includes that the software supports and is compatible with IAS, including:

- Identifying where a contract, or series of related contracts, should have Hedge or Equity accounting rules applied
- Recording specific details related to Hedge transactions
- Mark-to-Market revaluations of forward, long-term and derivatives contracts
- Automatically generating General Journal entries, according to IAS rules, for electronic import into corporate General Ledger systems

Accounting Approaches

There are two broad accounting approaches that can be used for forward and derivatives transactions under IAS 39:

- **Hedge Accounting.** Forward and derivatives unrealised transactions are not posted to the Profit/Loss or Balance Sheet statements. The use of Hedge Accounting must be substantiated by proving that these transactions closely match an underlying exposure of the business. Conventions have been established for testing the effectiveness of the links between financial hedge transactions and underlying exposures. The challenge here is firstly measuring the effectiveness of the hedge transactions and secondly documenting the intention of the transactions.
- **Equity Accounting.** Using Equity Accounting rules the unrealised Profit/Loss (Mark To Market) of forward and derivatives transactions are posted to the financial accounts. The challenge here is calculating accurate Mark To Market results for a broad range of often complex or exotic financial instruments and then automatically posting these figures to the corporate General Ledger system.

Corporate treasuries will have to decide which accounting approach to take for forward and derivatives transactions under IAS 39. Many corporate treasuries will use a combination of both approaches. In the CAPIX software the use of Hedge or Equity Accounting can be defined at the Transaction Type and Unit levels. This provides a high level of flexibility and control. The amount of data and processing complexity for corporate treasuries will increase significantly with IAS 39. Informal systems such as spreadsheets will not be sufficient for this task and should be replaced by formal systems such as CAPIX Treasury Manager.

Hedge Accounting

Hedge Accounting is also commonly called "Off Balance Sheet" Accounting. This has been the most common approach of corporate treasuries prior to IAS 39.

Under Hedge Accounting the unrealised gains or losses from forward and derivatives transactions are not recorded in the corporate Profit/Loss or Balance Sheet accounts. Ideally these unrealised gains and losses should be quantified and included in the notes attached to the financial accounts. In practice these unrealised Profit/Loss results are commonly not measured due to the complexity and difficulty of their measurement.

Under IAS 39 this has changed and Hedge Accounting can only be used if the documentation substantiates that the forward and derivatives transactions effectively cover an underlying financial business exposure. Conventions have been established for testing the effectiveness of the links between financial hedge transactions and underlying exposures.

All links between hedges and exposures need to be clearly identified and documented. This can be achieved using the Exposure Analysis functionality in the CAPIX software.

Cashflow Matching

CAPIX uses a "Cashflow Matching" methodology for evaluating the effectiveness of hedge transactions. The system manages this by matching the cashflows for the exposures against the cashflows of the hedges:

Reporting based on Exposure Analysis Strategies uses the size and timing of cashflows to measure the strength of correlation between the underlying exposure and the treasury hedge transactions using common measures such as the "80/120" rule. CAPIX reporting is designed to provide a documentation trail for substantiation of Hedge Accounting.

Description	Reference	Date	Amount Allocated	Notes
FX Forward Cover Contract New	FX-X-00006	25/10/2004	2,000,000.00	
FX Forward Cover Contract New	FX-X-00007	25/10/2004	1,000,000.00	
FX Forward Cover Contract New	FX-X-00008	25/10/2004	2,500,000.00	
FX Forward Cover Contract New	FX-X-00010	25/10/2004	500,000.00	
FX Forward Cover Contract New	FX-X-00011	25/10/2004	3,000,000.00	
Machinery Purchase	235689	25/10/2004	(10,000,000.00)	
FX Forward Cover Contract New	FX-X-00012	25/10/2004	1,750,000.00	

Equity Accounting

Using Equity Accounting rules the unrealised Profit/Loss (Mark To Market) of forward and derivatives transactions are posted to the financial accounts.

The challenge here is calculating accurate Mark To Market results for a broad range of often complex or exotic financial instruments and then automatically posting these figures to the corporate General Ledger system. This can be achieved using the General Ledger Integration module in the CAPIX software.

When implementing the CAPIX system, rules are defined to map various types of transactions to the relevant accounts from the General Ledger Chart of Accounts. Typically this will include foreign exchange rates and yield curves for debt instruments. These market values can be manually input or imported electronically.

Mark-to-Market values can then be calculated on open positions and these amounts posted as General Journals to the General Ledger.

Assuming the corporate General Ledger Chart of Accounts has been structured appropriately and that the CAPIX G/L Mapping rules have been defined properly, this process of posting Mark-to-Market General Journals will support the use of Equity Accounting for forward and derivatives treasury transactions.



All CAPIX software packages have been engineered using familiar Microsoft® technology and integrate seamlessly with Microsoft Office® products such as Excel® and Word®. This means deploying CAPIX software is quick and easy in modern corporate environments.