Coalition for Derivatives End-Users, a group whose members include the Business Roundtable, the U.S. Chamber of Commerce, and Financial Executives International.

Under Title VII of the Dodd-Frank Act, regulators, including the Commodity Futures Trading Commission, the Securities and Exchange Commission, and the Federal Reserve, have to write new rules to bring OTC derivatives under the regulatory umbrella. As part of those regulations, rulemakers are weighing new capital and margin requirements on cleared and non-cleared transactions for swap dealers and major swap participants. Corporate end-users have been lobbying for an exemption, but it's still unclear how they'll be affected by the rules.

Having to post cash margin will hurt end-users' ability to manage their day-to-day biz risks, said David Hirschmann, president and CEO of the Chamber's Center for Capital Markets Competitiveness. Those firms will have to choose whether to tie up their working capital, to "go naked and simply not manage their risks," or try to find other jurisdictions to transact, he said during a Feb. 14 call with reporters.

Of the 74 BRT and U.S. Chamber companies responding to the survey, 97 percent (72 companies) reported the use of OTC derivatives. The companies report using 62 percent of their derivatives to manage interest rate risk; 27 percent to hedge foreign currencies; and 16 percent to hedge commodity prices.

The requirements could potentially shift some hedging activities overseas, Marie Hollein, president and CEO of Financial Executives International, noted. Among those surveyed, 46 percent of respondents indicated that they would evaluate the ability to transact in foreign jurisdictions as a result of U.S. OTC restrictions.

Most respondents (91 percent) said transactions costs associated with trading would likely increase due to higher margin and capital costs placed on counterparties. In response to higher costs, 68 percent of firms said they would likely reduce hedging, while less than a third would likely continue their current level of hedging. Roughly three-quarters of the firms (77 percent) said they would consider alternative means of managing risk, while 41 percent would increase pricing to end customers, and 23 percent would shift risk to customers or suppliers, according to the survey results.

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Among 66 companies that provided data on the notional amounts of their OTC derivatives exposure, the total gross notional amount was $422.2 billion, or $6.4 billion per company, a median of $730 million. With no exemptions, a 3 percent margin requirement would result in aggregate collateral of $12.7 billion, or $191.9 million per firm on average, roughly 1 percent of revenue, according to the report.

> "The requirements could potentially shift some hedging activities overseas."
>
> — Marie Hollein, President and CEO, Financial Executives International

Coalition members say it's still unclear whether the CFTC will exempt end-users from the requirements. In Feb. 10 written congressional testimony, CFTC Chairman Gary Gensler said transactions involving non-financial entities don't present the same risk to the financial system as those solely between financial entities. Consistent with that, he said proposed rules on margin requirements "should focus only on transactions between financial entities rather than those transactions that involve non-financial end-users." Although Gensler has indicated that the CFTC has the authority to exempt end-users, Hirschmann noted that the CFTC chairman "hasn't stated a commitment to do so."

Coalition members say the ultimate impact on end-users of any exemption will depend largely on what the Federal Reserve does, since the Fed that sets margin rules for bank swap dealers, which account for the vast majority of hedging transactions done with end-users. It's also uncertain whether clearing charges imposed on financial institutions could be passed on to corporates in another way.

The issue has also caught the attention of several Senate lawmakers. In a Feb. 8 letter to the leaders of the Treasury, CFTC, SEC, and the Federal Reserve, a group of 13 senators, including Sen. Mike Johanns, R-Neb., warned that imposing margin requirements on companies that engage in hedging of legitimate business risk would "not only blatantly disregard the end-user exemption and Congressional intent, but it could also have the effect of draining scarce working capital from the balance sheets of mainstream American companies." ■

—Melissa Klein Aguilar

Anticorruption Trends: What You Should Expect in 2011

A reminder for compliance professionals who believe they've got Foreign Corrupt Practices Act compliance in the bag: Don't forget to do a regular gut check.

It's often said, but it bears repeating: That program you have in place only works if it's properly implemented and monitored. "Companies often put a program in place and think they've done their job, but day-to-day nobody's checking that it's working and being used," says Stuart Altman, a partner in the law firm Hogan Lovells.

Given the current anti-corruption enforcement climate, being able to demonstrate that your program is actually being used is even more important than ever, Altman says. That means having someone—whether he be a compliance, internal audit, or an outside consultant or vendor, conduct periodic checks to make sure the program is operating as intended. It also means keeping a record of any due diligence to be able to show that the company took the proper preventative measures to avoid a problem if one should arise.

Altman also shared his views on FCPA enforcement trends compliance executives should keep in mind. Most notably, big in-

vestigations, big cases, and big penalties are here to stay. The latest enforcement statistics are proof that the Department of Justice is delivering on its promise of increasingly aggressive FCPA enforcement.

"2010 marked a real change in both volume of cases and the way cases are investigated," says Altman. While past years saw one or two marquee enforcement actions accompanied by a flurry of smaller actions, last year marked a succession of high-dollar value settlements and penalties across a range of cases. Indeed, eight of the all-time 10 largest FCPA penalties in history were handed down in 2010. Altman expects that to be the rule, rather than the exception going forward. "The days when a company could get off with a relatively small fine and a promise not to do it again are gone," he says.

Enforcers are aggressively pursuing FCPA investigations, as evidenced by the 2010 FCPA sting operation that resulted in the arrest of 22 people. And where they do find a case, they're quick to expand their investigation to other companies.

Companies should also be prepared to conduct more investigations into alleged FCPA violations thanks to the new Securities and Exchange Commission whistleblower bounty program being established under the Dodd-Frank Act. "Companies have to be prepared to do thorough investigations to prove a spurious complaint," says Altman.

Non-U.S. companies in particular ought to shore up their compliance efforts. While those companies are increasingly the target of FCPA enforcement actions, "A lot of companies with minimal ties to the U.S. operate under the belief that they're free from concerns about FCPA compliance and don't have strong compliance programs in place," says Altman. Nearly all of the largest Justice Department enforcement actions in 2010 were against non-U.S. companies.

Thanks to increased cooperation, resources, and coordination, companies should expect more follow-up on cases—both within the U.S. and from foreign enforcement agencies. Where the Justice Department brings a case, the SEC often follows and vice versa. As U.S. enforcers increase their coordination and cooperation with their foreign counterparts, such as the United Kingdom's Serious Fraud Office, companies will face global anti-corruption enforcement. ■

—Melissa Klein Aguilar

CPAs Calling for U.S. Audit Guidance on Valuation

In the absence of any fresh guidance in the United States about how to audit valuations of complicated or illiquid financial assets, U.S. accountants are grateful to see something perking on the international front.

The International Auditing and Assurance Standards Board is finalizing an audit practice statement proposed last October that would give auditors some new guidance on using specialized skills or knowledge as part of the audit process, especially as it relates to valuing complicated financial instruments.

The guidance also addresses auditing procedures and timing, communications with regulators, and credit risk, especially when valuing financial liabilities.

The New York State Society of CPAs says market conditions, interest rates, and credit quality all have a "profound impact" on the valuation of complex financial instruments. The IAASB's proposed guidance would help a great deal in clarifying how auditors can get a better understanding of all the relevant elements that go into such valuations, the group says.

In fact, the United States could use a refresher on the same topic, says Anthony Chan, a partner with accounting firm Berdon and chair of the NYSSCPA's SEC Practice Committee. "Do we need guidance in the United States? Absolutely," he says.

Chan notes the last substantive guidance offered to U.S. auditors came from the Public Company Accounting Oversight Board in the form of Staff Audit Practice Alert No. 2 published in December 2007 and Alert No. 4 published in April 2009. The PCAOB has nibbled at the edges of valuation issues with other alerts addressing economic conditions, using the work of outside auditors, and unusual transactions.

Chan notes auditors might gain some meaningful insight by reviewing the international guidance and considering it when auditing U.S. GAAP financial statements. But caution is in order, he says, because the guidance doesn't have authority in U.S. capital markets.

> "The challenges are not unique to international audits. Some guidance for U.S. auditors would be helpful at this point."
>
> — Anthony Chan, Partner, Berdon

"The challenges are not unique to international audits," Chan says. "Some guidance for U.S. auditors would be helpful at this point." ■

—Tammy Whitehouse

IRS Offers New Chance to Report Offshore Assets

For companies or individuals who haven't yet come clean about offshore assets and accounts hidden from U.S. tax, the Internal Revenue Service is offering a second chance.

The IRS recently rolled out a second voluntary disclosure program for any taxpayer—corporate, individual, or any other entity—with unreported income from offshore assets and accounts to catch up on the tax and potentially avoid criminal prosecution. The IRS first smoked out some 15,000 taxpayers with a similar initiative in 2009.

According to the terms of the voluntary disclosure program, taxpayers who choose to step up will be required to pay any unpaid taxes, interest, and penalties for the last eight years. They'll also pay a special 25-percent penalty beyond any other penalties that might apply.

It's a little more onerous than the terms of the 2009 voluntary disclosure program, but that's to avoid rewarding anyone who chose to wait, says Michael Zargari, a partner with law firm Herrick, Feinstein. "If hypothetically the IRS subsequently decides to have a