Treasury Centralization in Asia Pacific

Treasury and Trade Solutions

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Foreword

Companies today face unique challenges on multiple fronts. These range from uncertainties in the global macroeconomic outlook, evolving regulatory and tax landscape, rapidly changing technology and a volatile business environment. Against this backdrop, treasury and finance leaders are actively looking for transformational growth opportunities – to improve working capital, increase operational efficiency, and create new sources of value.

In Asia, treasury centralization is a rapidly evolving trend for many of our clients as they focus on liquidity and funding in the most cost efficient manner. We see global multinationals moving their treasury centers to the region, in particular Shanghai, Singapore and Hong Kong. We also see increasing global expansion of large Asian corporates, along with needs for centralized structures to optimize liquidity flows – whether by simplifying payments processes, establishing shared service centers, or implementing technology solutions to drive treasury automation. Managing the varied local growth and regulatory complexities have led to the development of hybrid structures integrating local, regional and global businesses. Currently, Citi supports over 4,000 concentration structures in Asia, and this number continues to grow.

Corporate treasurers manage a dynamic environment and need to have treasury practices which are sustainable in the long term yet flexible to manage the diverse changes along the way. This report on *Treasury Centralization in Asia Pacific* provides insights on how companies can capitalize on key regulatory, market, and tax changes to implement best-in-class treasury and liquidity management strategies. We have also included case studies that capture much of the essence of our recent work with clients, supporting their priorities to improve funding efficiency, optimize liquidity and cash flows, and automate processes.

We hope you enjoy reading our report as a source of inspiration. Please do not hesitate to let us know if there are specific areas of interest that you would like further dialogue on.

In Asia, treasury centralization is a rapidly evolving trend for many of our clients as they focus on liquidity and funding in the most cost efficient manner.

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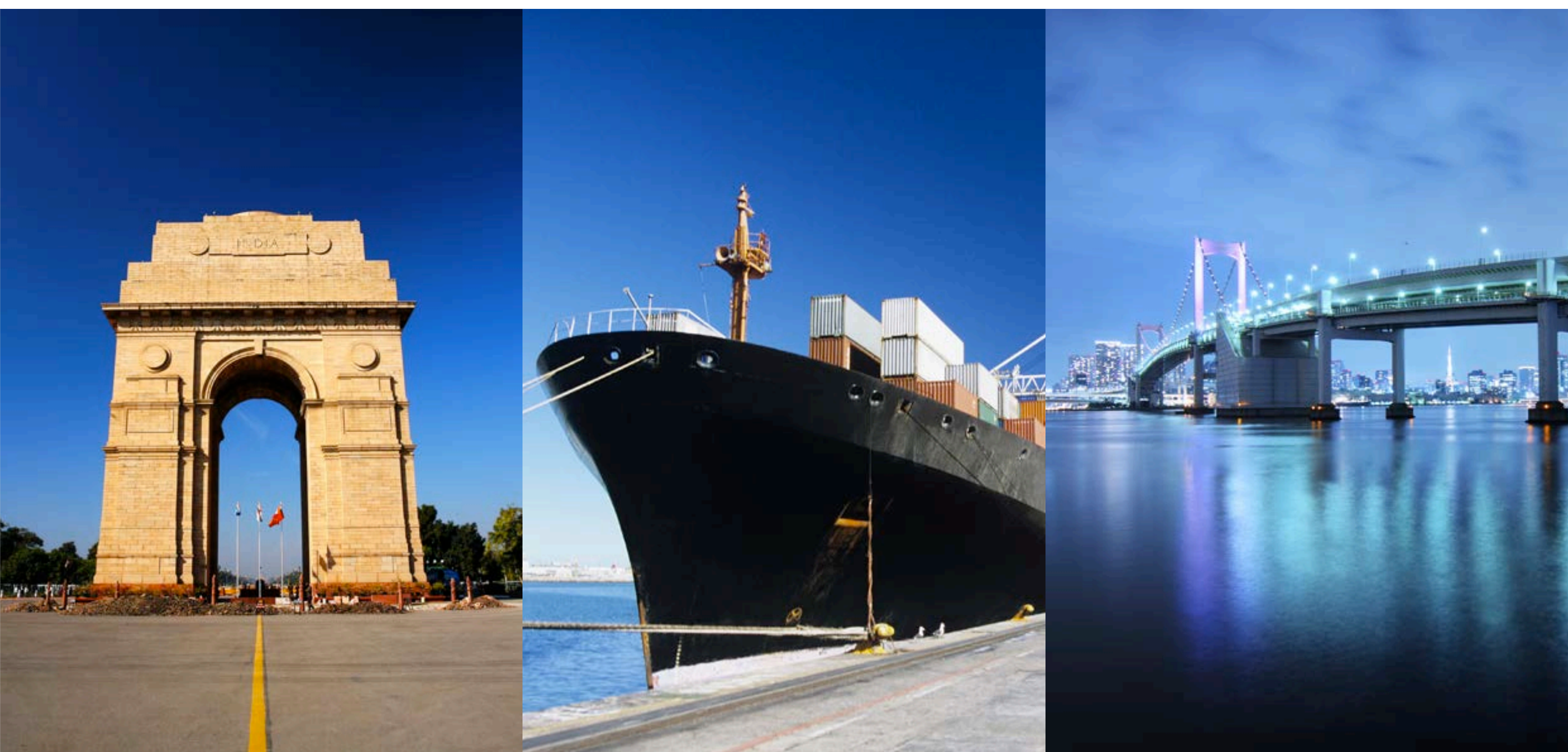

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Navigating Regulations, Rates and Risk in Asia

In the swirl of banking regulatory and interest rate changes taking place in Asia Pacific, demands on corporate treasurers are intensifying. What key trends should they look out for in 2016 as they navigate a landscape marked by diverse legal frameworks, economic systems, commercial languages and banking infrastructure? **Nishami Dharmaratne**, Head, Regional Liquidity and Investments Solutions, Multinational Client Segment, Asia Pacific, Treasury and Trade Solutions, Citi, and **Deborah Mur**, Asia Pacific Industrials, Energy, Power and Chemicals Sector Head, Treasury and Trade Solutions, Citi, suggest where to start.

Trend #1: Interest Rate Environments

In 2015, we saw 24 rate changes across key markets in Asia. Since entering 2016, we have had another eight rate cuts — and counting — with the most recent being the the Reserve Bank of Australia announcement on May 3 that it had reduced the target interest rate by 25 basis points. Often, inflation considerations are the main reasons for such actions by central banks.

The impact of these rate cuts to economic constituents, which include individuals, companies, governments and many other organizations, is considerable. In 2015 alone this amounted to 6% in value reduction in Asia, which they would otherwise have been able to create through their assets earnings, or through liquidity optimization. This is a phenomenal change compared to the last decade, where interest rates were generally high in most Asian markets.

This is one of the dilemmas faced in managing treasury today — understanding the rate environment, what strategies you can adopt, which solutions, tools and platforms are best for your organizations in dealing with these uncertainties, and what methods treasurers can deploy in bringing that value back to their organizations.

For some treasurers, it could be better refinancing of short to medium-term debt, or widening the range of investments with a view to gain higher yield. For others it could be a simple optimization of liquidity.

While the objectives can vary, the starting point can be an honest evaluation as to where your cash is – is it in the fungible markets you can move, or is it in trapped markets? Is the cash used well domestically, or is there a need to look at transfers, or lending out to HQ or another subsidiary? Then, if you actually have the right solutions and systems in place to manage, you can gain visibility.

Rates cuts are one salvo in the monetary policy arsenal – the other new development is negative interest rates. For some markets, this is a chance to reinvigorate their economies when all other monetary policy tools are exhausted. This is an unorthodox view, ushering in a new era for central banks globally.

Negative interest rates is something we have seen more from Europe, but their implications are far broader. Within Asia, Japan has been the latest to join the stream. In January 2016, when the Bank of Japan announced its negative rate policies, financial markets went into a frenzy, even though the policy applied mainly to selected current account deposits that banks held with the Bank of Japan.

Since the announcement, Japanese government bonds have seen volatile price swings, mainly with longer-dated instruments.

However, it is important not to make assumptions, as the way negative interest rates have been implemented reflect how the practice in each market can be very different. The general expectation is that banks would review the impact and possibly implement charges for those deposits held in the currencies that are yielding negatively. Some regulators recognize the concept, but are struggling to understand the execution of it, so there can be variations in the process.

China and Korea for example, are not necessarily considering whether banks can go ahead and impose a charge, but are reviewing the best approach for this concept.

What is more important for the treasurer is carefully examining the billing currencies, understanding the charge methodologies in each market, and evaluating the pros and cons of liquidity held in these currencies. Do not forget to consider the long-term view of these currencies before decisions are made.

Trend #2: Varying Degrees of Regulations

One significant regulatory impact that is well-known is Basel III, which is primarily a measure to ensure banks are safe and sound from a capital, leverage and liquidity perspective. While this is mainly a banking regulation, corporates will start to feel the impact as their partner banks begin adopting various strategies to deal with it. In particular, both short-term (less than 30 days) and long-term (beyond 1 year) views on liquidity measures will become extremely important to banks.

This means that banks will closely monitor the deposit values and operational nature of the bank accounts, and the level of stability of the deposits. Treasurers will need to evaluate the value of the deposits created and what the core liquidity is, versus strategic liquidity.

The treatment of these two types of liquidity can be different – hence earning power can vary.

Another factor for consideration is the general regulatory environment itself, which affects the way companies operate. This is particularly complex in Asia, where there are nearly 16 markets, all of which have their own legislative systems, tax systems and company legislations which define many different intercompany rules, thin capital thresholds, and numerous commercial guidelines.

Take for example, Vietnam's announcement last year that US dollars will not attract any interest onshore. If yours is a USD-invoicing company, your onshore USD liquidity will no longer attract any yield.

Or consider Indonesia. Indonesian requirements are increasingly focused on commercial transactions. For a start, every commercial contract in Indonesia must be in the local Bahasa language. Secondly, every commercial transaction needs to be settled in Indonesian rupiah. If you are a dollar-based company, you are typically invoicing in dollars, which was allowed in the past, but is no longer the case. You will need to consider better ways to draft your invoices, collect in local currency, then decide what to do with the rupiah once you have collected it.

If companies do not have the on-ground expertise or the footprint to deal with that, they can turn to a banking partner who is equipped to support them and provide solutions.

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Over in India, the Companies Act 2013, which restricts the ability of private and public companies to conduct intercompany lending if they share the same directors, makes multi-entity pooling a challenge. However, we have found that more companies are exploring multi-bank cash concentration to enhance their domestic liquidity management efficiency.

By that same token, countries like Thailand had introduced recent relaxation measures and treasury incentives to facilitate fund flows into Thailand. Extracting liquidity out of the country for optimization at regional or global levels is still a challenge, but these are a welcome start.

Trend #3: Liquidity Transferability and Convertibility

We have observed a spectrum of markets within Asia's regulatory landscape. There are the developed and flexible domestic and cross-border markets of Singapore, Hong Kong, Japan, Australia and New Zealand. And there are the semi-regulated markets such as Indonesia, Malaysia, Philippines, and China, where the view on transferability of their currency and convertibility of the currency is somewhat restrictive.

How transferable a currency is, and how flexible it is in terms of convertibility, creates opportunities for companies. The good news is that more and more markets are opening up, as in the case of China and Thailand.

But some countries are still viewed as trapped markets — these would include India, Vietnam and Bangladesh, amongst others. If you enter these markets, where you need to have some self-funding arrangements, it would make a lot of sense to look at a domestic solution in those countries, and have a buffer of regional pool.

In a landscape like Asia's, a corporate should define what the best liquidity optimization strategy would be — whether it should be a domestic solution to support the business model in trapped markets, or potential regional solution for the fungible markets where liquidity is easily transferable.

When it is a restricted or semi-restricted market, companies can keep some or all of the cash in the country to meet their liquidity needs, given the challenges associated with cash forecasting or time zones. Corporates can avoid potential loss of value when they choose in-country centralization options. On the other hand, where companies have the flexibility to co-mingle liquidity amongst multiple entities and multiple countries, then they can opt for regional or global pools.

Looking Ahead

As treasurers navigate an uncertain landscape, the vision is for flexible cash management systems, which at the minimum support their day-to-day cash management operations. Treasurers should also ask if the solutions they have today allow them to stretch themselves, to leverage opportunities that will enhance use of liquidity, and achieve better yield, with the end objective being to put in place the optimal liquidity structure.

They should also evaluate liquidity in terms of operational and strategic cash, and form a view on whether strategic cash is needed in the short run, or whether it can be deployed with high-yield instruments for the medium or long-term. This allows a treasurer to enhance earnings from excess liquidity.

In day-to-day liquidity requirements, what companies are increasingly looking for is speed and efficiency of liquidity solutions. Therefore having the right banking partner who can provide the best possible platform, giving you very quick service in the movement of your cash, whether it is globally, regionally, or in-country, is important.

In most cases, we find companies are also increasingly looking at the depth and breadth of products and solutions, which can support multiple currencies, multiple entities, multiple residencies, and multiple countries, with a view to mobilizing their liquidity effectively.

In summary, treasurers should keep three primary goals in mind when navigating this ever-changing landscape: operational efficiency, integration, and the optimization of liquidity.

Treasurers should ask if the solutions they have today allow them to stretch themselves, to leverage opportunities that will enhance use of liquidity, and achieve better yield.

Bank Account Rationalization: A Numbers Game?

As economic realities, market progress and industry diversification continue to underpin the focus of corporates on financial efficiency, corporate treasuries are increasingly driven to examine their bank account structures to reduce associated fees and expenses, enhance cash visibility, improve control over cash and deploy surplus cash to fund growth and investment.

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This first edition of a three-part series on bank account rationalization looks at the strategic landscape and key considerations of merging the accounts payables (AP), accounts receivables (AR), payroll, tax and treasury flows into a single physical bank account per country and/or legal entity. The subsequent editions in the series will focus on the on-behalf-of (OBO) models and the potential benefits of adopting virtual bank accounts.

The Balancing Act

Conventional wisdom dictates that the fewer the bank accounts, the greater the financial efficiency. However, this may not always ring true as corporates going through transformation-type projects have to balance between considerations of operational and financial efficiency.

While any assessment of bank account structure often leads to a review of the number of physical[1] bank accounts, the chief question on corporate treasurers' minds has evolved from "What is the *lowest* number" to "What is the *optimal* number" of accounts to be held with banks. The ultimate number would depend on whether one single bank account per country and/or legal entity is sufficient for the efficient and effective processing of account payables, account receivables, payroll, tax and treasury flows.

Treasury transformations through centralization, standardization and automation provide significant benefits around operational efficiency and control, and help reduce overall processing cost through a common technology backbone. Nevertheless, when the number of physical bank accounts is simply too high, this will result in greater challenges around managing positions and balances, in addition to potentially sub-optimal liquidity structures and additional overall costs. For instance, a decentralized operating or growth model through mergers and acquisitions may result in marginal central design around the underlying bank account structure, which could lead to a large number of bank accounts. Based on Citi's analysis, it is estimated that the average cost of maintaining a physical bank account is USD5,000 per year, factoring in costs of account maintenance, reporting, reconciliation, audit certification and internal year-end audit. Assuming the global average number of bank accounts per company is 224,[2] and given a company rationalizes approximately half of the accounts, this would result in a potential annual cost save of ~USD500,000.

One Size Fits All?

Recognizing the constant pressure to improve both operational and financial performance, a physical bank account structure should seek to:

- Enhance the visibility of cash
- Increase the control of cash
- Improve the efficiency of cash

Maintaining an optimal number of physical bank accounts may reduce overall administrative effort, decrease costs and could mitigate risk by virtue of simplifying visibility over regional and global cash positions. Furthermore, an optimal number of bank accounts could provide a more streamlined and efficient liquidity management structure, which may enable timely action in volatile market environments.

Whilst a single physical bank account per country and/or legal entity to support both transactional and treasury flows sounds like the ideal model from a simplicity perspective, one size does not fit all. It is important to fully analyze the nature and volume of flows, the significance of certain flows from a regulatory or confidentiality perspective and the time-

[1] A physical bank account refers to accounts with banks which are not "virtual" accounts.

[2] The global average number of banks accounts per company is sourced from a Visa whitepaper titled "*The Cash Flow Visibility Index: A diagnostic tool for risk & liquidity benchmarking*," based on a 2014 survey commissioned by Visa and researched by East & Partners Asia, covering 811 corporates across 10 countries globally.

sensitivity of information flows for certain processes (such as daily cash positions). In these scenarios, efficiency and potential savings are germane to the bank account rationalization process.

Before making a conclusive verdict on the bank account rationalization process, here are several considerations treasuries need to think through:

1 Operations and control:

- Reviewing the payment and collection instruments required by the supported business units, in terms of their end-to-end process, will help mitigate challenges which typically arise as part of the returns process. For instance, whilst payroll transactions may be processed with a bulk debit entry on the bank statement for confidentiality reasons, returns could be processed and applied individually.
- Understanding who ultimately has responsibility for reconciling the physical bank account is very important as various teams could be working on an account in parallel. The process of segregating discrepancies and identifying ownership could lengthen the reconciliation process.
- Reviewing current treasury timings around account positions and timings for existing AP and AR reconciliation will help to determine if merging all transactional and treasury flows makes sense. If the bank reconciliation teams are reconciling flows for AP and AR on the same physical bank account, treasury will potentially be forced to wait longer in the day before decisions can be made.
- Assessing treasury's risk management activities will help to plot how processes can coexist under a single country level physical bank account model. Whilst technology could enable this type of 'one' physical bank account model, separate accounts could enable a more timely and efficient treasury reconciliation process and merging accounts may actually be counterproductive.

2 Technology:

- Bank technology capabilities to support multiple user access rights for account maintenance is vital to ensure smooth operational efficiency.
- Understanding how the AR operational teams process returns is equally important. For example, there could be cases where only one user can work on a single account at any point in time within a specific ERP system. In this scenario, other members of the bank reconciliation team in the same nominated bank account will be idle until the re-work is complete.

3 Regulation:

- Regulatory stipulations in certain jurisdictions may lead corporates to preserve distinct bank accounts for each of their legal entities.

4 Bank relationships:

- The number of banks with whom corporates have credit facilities could have a direct bearing on the rationalization process. For instance, it is generally observed that banks issuing documentary credits require that trade payments be effected through them.

5 Others:

- Preferences of key customers or suppliers to utilize accounts with specific banks may factor into the thought process.
- Confidentiality around underlying visibility and control in marketsensitive scenarios such as mergers and acquisitions will also affect the control environment.
- Geographic coverage and the scope of transactions contemplated through the account may add additional complexity especially when consideration is given to forecasting and management reporting processes.

What's Next?

Notwithstanding the multitude of factors treasuries should evaluate when they embark on a physical bank account rationalization project, a partner bank with the necessary experience and know-how is essential to establish the most efficient cash management model.

Even as maintaining a smaller number of physical bank accounts may mitigate risk and could reduce overall administrative effort and costs, determining the level of physical bank account rationalization may be more important to eliminate counter-productivity. While the merging of all transactional and treasury-related flows is technologically possible, the associated operational, control, regulatory, relationship and confidentiality requirements needs must be fully understood before the optimal physical bank account structure can be determined.

Notwithstanding the multitude of factors treasuries should evaluate when they embark on a physical bank account rationalization project, a partner bank with the necessary experience and know-how is essential to establish the most efficient cash management model.

Notional Pooling: A New Era

Notional pooling has traditionally been popular amongst multinational companies as an effective liquidity management tool, supporting "the right amount of cash to be in the right place, at the right time". By offsetting debit and credit balances on a notional basis, corporate treasurers are able to manage regional and global cash positions without having to conduct intercompany lending or incur costs from foreign exchange conversions.

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In recent years, evolving regulatory, tax and accounting issues have resulted in tightening requirements around notional pooling. In this article, we explore the implications of these changing dynamics on banks and their corporate clients. Are banks changing their views on notional pooling? What evaluation criteria should corporate treasurers use when setting up notional pooling structures in the new regulatory environment? Are there other liquidity management techniques that enable treasurers to achieve similar objectives?

Understanding the Impact of Regulatory Evolutions and Accounting Principles

Basel III guidelines

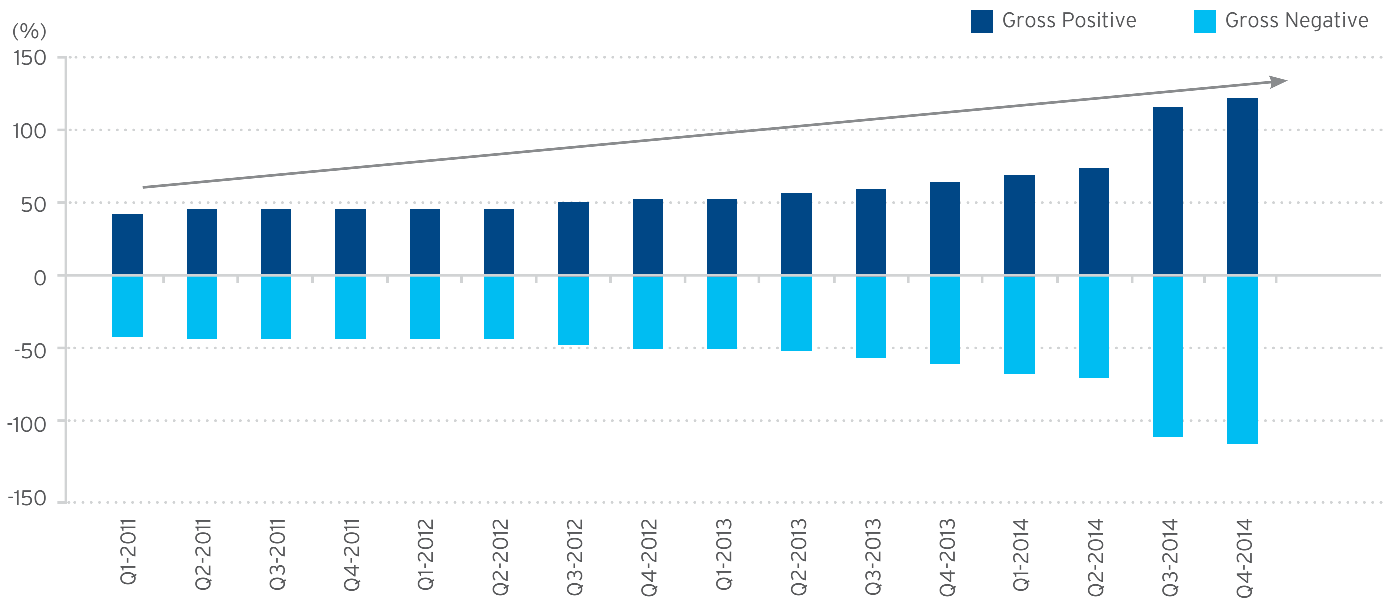
Basel III and its equivalent local variations such as the Capital Requirements Directive (CRD) IV in Europe, and implementations by the Australian Prudential Regulation Authority (APRA) and Hong Kong Monetary Authority (HKMA), generally look to strengthen bank capital requirements by requiring banks to ensure sufficient liquidity and adequate capital to decrease bank leverage. Thus, with the impending implementation of Basel III, banks are continuously reviewing the scope of banking services they provide in tandem with pricing and cost conditions under Basel III.

Notional pooling as a bank services product could have negative implications under the Basel III principles and its local variations in two key areas:

1 **Interpretation that banks may not be able to net off loans with deposit positions**
Notional netting of the balance sheet for the benefit of intra-group liquidity concentration is the basic premise of notional pooling.

Efficient Balance Sheet Usage

Notional pools integrated with operating activities have a more efficient balance sheet usage compared to overlay structures



There is less reliance on bank credit lines since overdraft positions can be offset against surplus cash positions to alleviate short-term funding mismatches. Basel III is expected to impact how banks offer notional pooling structures to corporate and institutional clients as it is now costly for them to set aside capital against overdrawn accounts. The implementation of Basel III may also be stricter in certain jurisdictions, for example under the APRA's guidelines, where there is a 100 percent Liquidity Coverage Ratio (LCR) on banks.

What's more, as notional pooling structures are typically overlay structures, excess cash buffers of entities that treasurers maintain in the pool may be deemed as 'hot money' alongside the capital costs attracted by the negative balances in the leverage ratio calculation of the pool. Overall, this may attract additional costs to the notional pooling structures.

2 **Distinction between core operating deposits and non-operating deposits (i.e. liquidity value)**
Basel III principles are designed to ensure banks have a sufficient cash buffer in place to cover numerous and sudden withdrawals. As a result, operating deposits linked to transactional and payment activities have increasingly gained in value. We have observed banks increasing their pricing for operating deposits thus improving LCR, and introducing new deposit products to support a more than 30-day liquidity coverage requirement.

As provided in the illustration, we have observed that notional pools that are integrated with operating activities have a more efficient balance sheet usage (and therefore lesser of a challenge for banks in substantiating LCR requirements) compared to overlay structures.

Consequently, there is a trend for banks which have typically supported pure overlay and foreign exchange solutions to start reviewing the costs structures of notional pooling solutions. This could result in increased costs, or legal reviews of existing structures.

Requirements of IFRS/IAS 32 versus U.S. GAAP

Under the International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) 32, bank account balances are deemed as financial instruments and therefore need to be disclosed and presented individually.

Applying the offsetting accounting requirements of IAS 32 can be complex as it represents the need for companies and banks alike to demonstrate the legal right and intentions to settle on a net basis[i].

[i] PricewaterhouseCoopers LLP on Cash-pooling Agreements, June 26, 2014.

Conversely, the U.S. Generally Accepted Accounting Principles (GAAP) continue to support the ability for banks to net the balance sheet. Thus corporates may start to see distinctions on how notional pooling programs are treated between European and U.S. banks as these banks start to re-evaluate existing structures and incremental considerations for applying notional pooling structures. For corporates implementing these structures, this may mean further legal and administrative burdens.

Potential impact of BEPS actions

The Organization of Economic Cooperation and Development (OECD) released its final Base Erosion and Profit Shifting (BEPS) Action Plan[ii] in 2015. BEPS aims to tackle tax planning strategies that exploit gaps and mismatches in tax rules to shift profits to low tax locations. Although not legally binding unless adopted at the local level, the BEPS Action Plan gives countries the tools to ensure that profits are taxed in the location where economic activities generating the profits are performed. In this regard, corporates that have implemented global or regional liquidity and funding structures, including notional pooling may be impacted by the adoption of BEPS actions in the countries where such structures operate. For instance, corporates may be subject to a greater level of business substance to enjoy a local tax incentive and/or double tax treaty benefits, as well as higher transfer pricing and reporting requirements. While we do not believe that the BEPS Actions should prevent corporates from setting up efficient liquidity structures, they may lead to incremental implementation complexities.

Considerations for Corporate Treasurers

While the various guidelines seem to spell the end of effective liquidity management practices, and in particular notional pooling, we do not believe this to be case. Here, we review some of the considerations and best practices to ensure long term sustainability of an efficient liquidity program:

- **Leverage alternative liquidity programs to achieve the same centralization objectives**
  As some banks re-evaluate the costs and feasibility of supporting a notional pooling program, corporates can also consider putting in place a physical cash concentration program where intercompany loans are created in order to centralize cash positions, or payment-on-behalf-of (POBO) and receipt-on-behalf-of (ROBO) programs which act to optimize cash efficiency within the in-house bank or treasury center. While these programs may demand additional elements of reporting and reconciliation as they involve physical accounting entries and require arms-length transfer pricing on intercompany loans, they serve as viable alternatives to corporates in light of incremental costs with notional pooling programs.

  Citi has been working with companies in Asia either looking to replace their notional pooling programs with physical cash concentration structures; and/or restructuring current solutions from multi-entity programs to single entity notional pools which would face a lesser challenge. POBO structures are also being reviewed as regulations are turning in favor of supporting these structures which underlie commercial transactions.

- **Select the most suitable header company and location**
  Driven by the Basel III, IFRS/U.S. GAAP requirements and BEPS Action Plan, it is our recommendation that the header company selected should have sufficient economic activities to justify the profits earned, either by way of treasury activities or via the pooling benefits. In addition, there will be increasing requirements from banks, in ensuring a 'clean pool' – i.e. one that has clear rights to set off between the positions, the header company should be incorporated in a location where there are clear rules supporting the right to set off, to show legality and intention to net the balances.

Corporates may start to see distinctions on how notional pooling programs are treated between European and U.S. banks as these banks start to re-evaluate existing structures and incremental considerations for applying notional pooling structures. For corporates implementing these structures, this may mean further legal and administrative burdens.

[ii] Organization of Economic Cooperation and Development (OECD), Base Erosion and Profit Shifting (BEPS) Action Plan, 2015.

In Asia, Singapore and Hong Kong are generally considered as the most suited locations for header companies within a notional pooling program in view of the availability of favorable treasury center tax incentives.

- **Apply additional due diligence on jurisdictions to be included for notional pooling**
  A general commonality amongst the various guidelines and regulations may be observed – there should be a clear legal right and intent present in order to net balances within the notional pooling structure. As banks start to impose these requirements on corporates, it is important for treasurers to ensure that there are clear legal rules which support the right of set off of balances within their company's notional pool.

  Likewise, while some banks like Citi already apply these practices, we would observe that all banks offering the notional pooling services would start to limit the product offering to jurisdictions where they have sought comfort on the legality of the right to set off.

- **Use one bank as a holistic cash and liquidity management provider**
  In alignment with the Basel III principles, some banks may start to apply incremental charges on negative balances in addition to reducing payout on excess balances within the notional pool structure. As a result, this would increase the cost of having a pool in place, which may start to outweigh the efficient liquidity management benefits that corporates enjoy today.

  Alternatively, corporates which have integrated the notional pool structure with the underlying operating business under one global or regional bank may not have these incremental costs under the Basel III framework. We encourage treasurers to ask their notional pooling bank how Basel III would impact their existing notional pooling arrangements.

In summary, there are many guidelines which vary across regulations, tax and accounting principles that could potentially impact the effectiveness of notional pooling structures as a liquidity management tool. While many treasurers may choose to use other liquidity management techniques such as physical cash concentration to centralize their cash positions, notional pooling still remains a viable solution. As banks look to reassess the conditions which the product is offered, it is important that treasurers are aware of the cascading implications to them, and act in a timely manner to apply appropriate measures to ensure a sustainable liquidity program.

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Redback Rising: Renminbi Trade Invoicing

According to the latest SWIFT tracker, renminbi (RMB) has advanced to the fifth position of most widely used currency for global payments. With the value of cross-border deals settled in the redback more than doubling in 2014, it is not surprising that more multinational companies are choosing to invoice in RMB as they look to improve profit margins.

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Opportunities for RMB cross-border trade settlement have developed rapidly since the first liberalization moves in 2009, and we see a growing trend towards the use of RMB for transactions. The latest SWIFT RMB Tracker data shows the Chinese currency has moved up from the 20th global payment currency to the fifth in the last two years.

Multinational companies (MNCs) are taking advantage of a number of benefits such as reducing foreign exchange (FX) risk and administrative costs, gaining from potential RMB appreciation, or expanding and strengthening relationships in their supply chain ecosystem. In fact, there is growing evidence that companies can improve their negotiating position with Chinese customers and suppliers when the Chinese currency is used for trade invoicing purposes.

While there are strong incentives for companies outside of China to transact in RMB, not all companies are prepared to jump on the bandwagon at this point. What are the considerations that treasurers need to evaluate before making the switch to RMB as an invoicing currency?

Key Benefits

For companies buying from China and selling overseas, especially MNCs executing intercompany transactions with their Chinese entities, settling such deals in RMB reduces exposure to FX risks. It also enables centralization of FX management at the regional, group or in-house bank level, which enhances economies of scale and improves pricing negotiation. For example, entities are able to receive proceeds settled in RMB earlier (versus foreign currency receipts in China), facilitating improved cash flow forecasting and negotiation for better pricing terms. Other benefits include potential discounting from third-party suppliers and access to a larger supplier base.

For companies sourcing from overseas and selling to buyers in China, there are benefits to be gained with a simpler documentation process

by using RMB (versus foreign currency payments), thus enabling a more efficient collection cycle and access to a larger customer base.

For MNCs with significant intercompany flows with China, there are benefits in centralizing the FX risks at an overseas function such as a treasury center or in-house-bank versus at the local Chinese entity, which may not have the know-how or primary responsibility to effectively manage FX positions.

Likely First-Movers

With the benefits in mind, the types of companies most incentivized to adopt RMB at present are those with manufacturing and sales in the Chinamarket. These companies are typically in the fast-moving consumer goods, healthcare and industrials sectors. Naturally, it makes sense for these companies to offset their operational expenses in the same currency that is generated from their revenue. In addition, due to the benefits from FX hedging, companies with significant intercompany flows with China have also been the first to review and make the switch to RMB.

On the other hand, invoicing in US dollar is still the more convenient choice for US-headquartered companies – they can eliminate FX risks by trading in their home currency. Other Western MNCs may find managing US dollar FX risk less challenging than managing RMB risk. Similarly, transaction flows from businesses, such as electronics or oil commodities, where China is part of the supply chain and not the only supplier or buyer, will continue to be denominated in US dollars.

Weak Currencies Bolster RMB Appeal

Recent depreciation of the euro has influenced the dynamic of European company's adoption of RMB. Volatilities in the European currencies and other weak global currencies have prompted some companies to gradually increase their use of RMB in a bid to diversify and mitigate FX exposures.

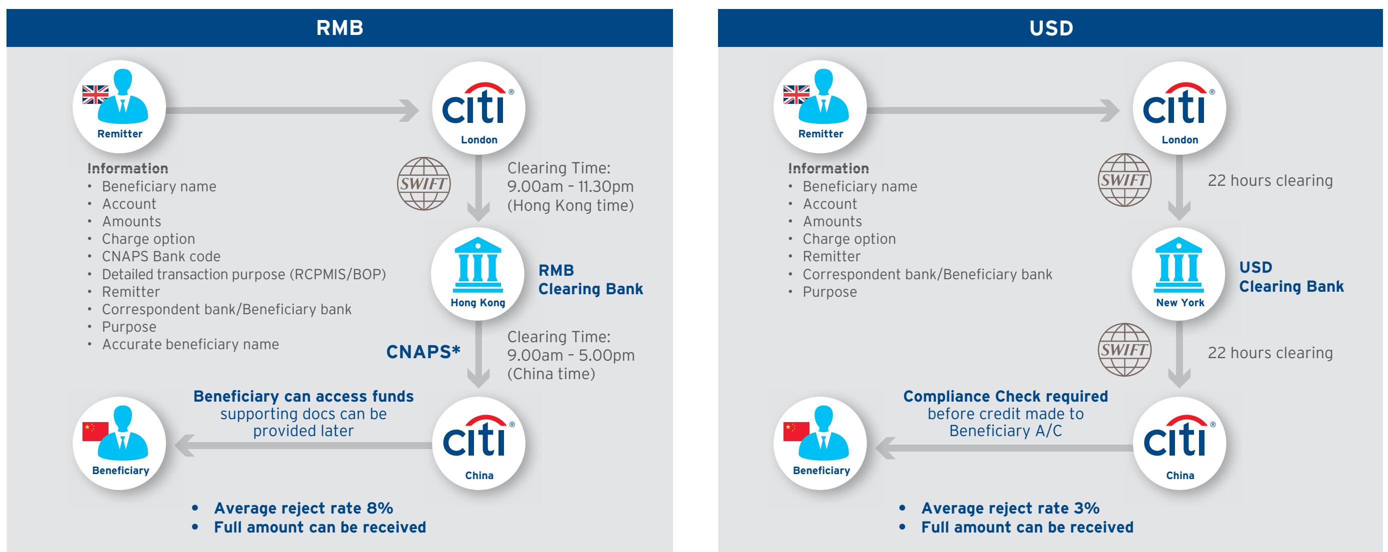
Before Making the Switch...

Changing an invoicing currency is never easy as this involves a comprehensive review across all relevant business units and systems. A company needs to ensure there is sufficient implementation resources assigned to execute the change, and the perceived benefits highlighted above are sufficient to warrant the costs incurred.

The change to RMB trade invoicing needs to be a long-term strategy as it cannot be easily reversed given the rules and regulations in China, and potentially high switch-back costs. The following considerations should be evaluated:

1 **Introduction of a new currency code – CNH**
With the existence of two currency codes for RMB, namely onshore CNY and offshore CNH, companies need to ensure that their treasury and dealing systems allow trading in CNH as a new currency. It is because any incremental risks, tenor availability and instruments available in accessing the CNH market needs to be considered in foreign exchange policies. Since the trade settlement currency for RMB remains as CNY, therefore, it creates potential currency/system conflicts which need to be reviewed.

Difference between RMB Clearing and USD Settlement



*China International Payment System is expected to improve the return/reject rate and enable more efficient clearing when deployed. Launch date to be confirmed.

2 Changes to trade documentation
While the RMB internationalization initiative has simplified process and cross-border controls are still in place, companies must understand the nuances for effective implementation. Supporting documentation such as the intercompany trade agreement, purchase order, place of acceptance authority document and invoice (*fa piao*), will need to be amended accordingly to ensure proper validation can be conducted by the relevant authorities in China.

3 Understand the RMB nuances
In addition to the necessity for supporting documentation, there are varying cross-border controls and processes in place for current and capital account activities. In this regard, there is incremental information which must be provided in the transaction messaging (versus foreign currency payments to China). This information and nuances are important to ensure that payments are not rejected, which affects the ability for companies to meet payment obligations on a timely basis and avoid external bank charges incurred by the Chinese entities.

4 Benefiting from different programs in China
Moving ahead from simplifying processes for current account activities, new payment programs also stemmed from the Shanghai Free Trade Zone (SFTZ) and nationwide initiatives, which enable companies to be performed on a net basis, or on-behalf-of. These programs allow companies to conduct payments with China on a more streamlined basis as they do in other more developed countries. However, certain nuances should be observed and they have been summarized in Table 1.

The RMB Journey Continues

Without doubt, RMB internationalization will accelerate and we will see incremental changes and flexibility offered by way of pilot programs such as Free Trade Zones, as well as improvements to cross-border controls and processes over time.

There will be potential tipping points for increased RMB invoicing going forward, and Citi continues to lead the way in helping clients to evaluate the opportunities created by ongoing regulatory reforms. At the right time and specific to a company's needs, RMB invoicing can certainly open new doors for companies – whether by negotiating cost savings or pursuing attractive new trading relationships with buyers or suppliers who are only willing to trade in RMB. The key is for treasurers to start preparing their companies to make the timely switch when the opportunity arises.

Table 1: Application of RMB Netting and On-Behalf-Of models: Onshore vs. Offshore

	Overseas Application	China Application	
		SFTZ	Nationwide
Parties involved	Typically intercompany	Allows customers and suppliers to be included	Intercompany only
Settlement – parties involved	Settlement between center and participants	On intraday basis. Leading company must be used as pass-through	On intraday basis. Settlement between netting center and participants
Settlement frequency	Usually monthly	Intraday basis	Usually monthly
Settlement account	On books of in-house bank Virtual settlement	Settlement must be through actual bank accounts	
Location of netting center	Centralized in single location	Leading company in China to act as pass-through for China participants	Domestic participants can settle with global netting center
Qualification criteria	Not specified	Leading company must be registered in the SFTZ	Only for qualified companies

Metamorphosis: Liquidity Management Landscape in India

India ascended to become the world's fastest-growing economy this year by clocking a GDP growth rate of 7.5%[1]. With strong growth and continued market development, India is emerging as a global powerhouse.

Mridula Iyer
India Cash Product Head, Treasury and Trade Solutions, Citi

Thus, it is crucial to understand the corporate treasury landscape and what it means when seeking for efficient liquidity management and corporate treasury landscape in the country.

Evolving Liquidity and Regulatory Landscape

Liquidity management has emerged as a strategic need for most organizations and organizations in this journey are at different stages of sophistication. Efficient liquidity management in India continues to be a challenging task given the ever changing payments and regulatory landscape. On a daily basis, corporate treasurers are faced with new challenges around managing risk and optimizing returns on cash flows.

In a recent survey conducted (Deloitte, 2015 India Corporate Treasury Survey), the top internal challenge cited by 83% of respondents continues to be the inability to obtain a clear view on exposures.

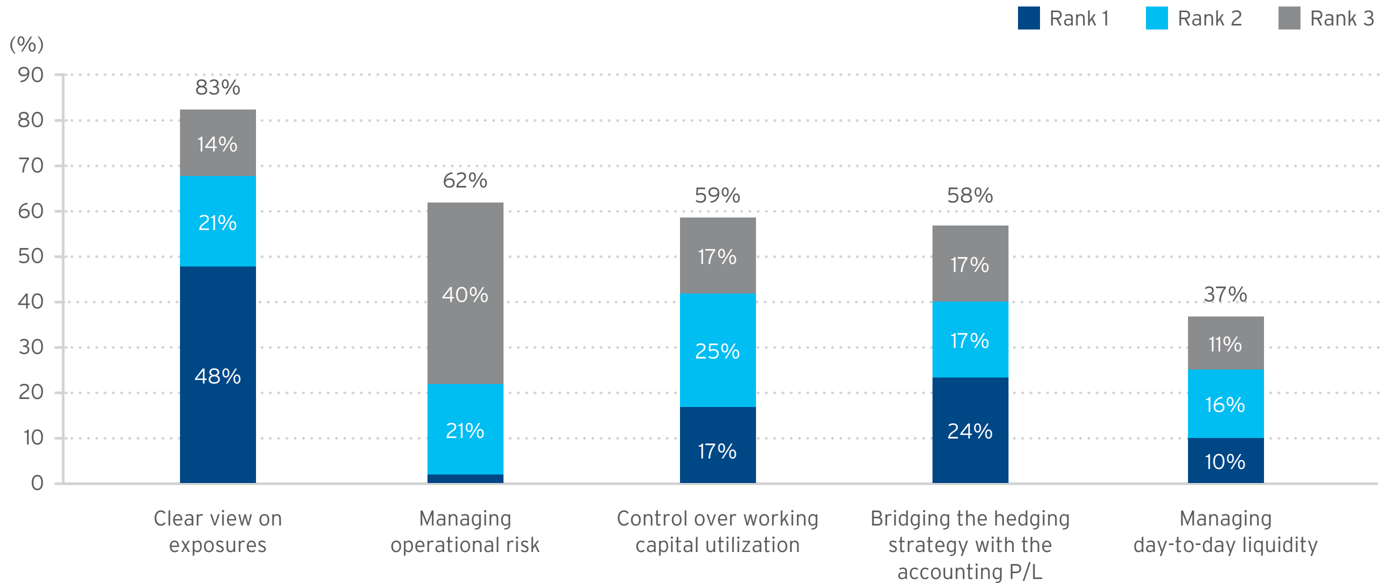
Due to the wide geographical landscape and differing capabilities across banks, corporates have traditionally worked with multiple banking partners. Adding complexity to the matter, a number of banks are unable to provide standardized account statements.

Further in India, automated and standardized payments messaging tools like SWIFT is not widely used between banks for domestic fund transfers. As a result, treasuries have to consolidate multiple statements and payment file formats often manually, leading to limited visibility and control on their account balances.

To manage this complexity, multinational companies operating in India are often then required to customize their global platforms for payments and liquidity management, thereby adding to their operating costs.

[1] World Bank report.

Internal Challenges in Treasury Management



Source: Deloitte 2015 India Corporate Treasury Survey: Excellence in Corporate Treasury Management

Intercompany loans have always been a popular working capital management tool for corporate treasurers globally, and in India, this is no different.

In 2013, changes to the Companies Act made intercompany lending and borrowing cumbersome between group companies. However subsequent amendments in May 2015 have provided some relaxation for private entities to conduct intercompany transactions, thus enabling corporate treasurers to actively start evaluating multi-entity cash concentration structures for optimizing their working capital requirements in India.

As such, in a survey conducted in Deloitte's 2015 India Corporate Treasury Survey, while Taxation and Companies Act related laws continue to challenge respondents in India, these regulations were deemed necessary in the given environment.

Unlocking the Value

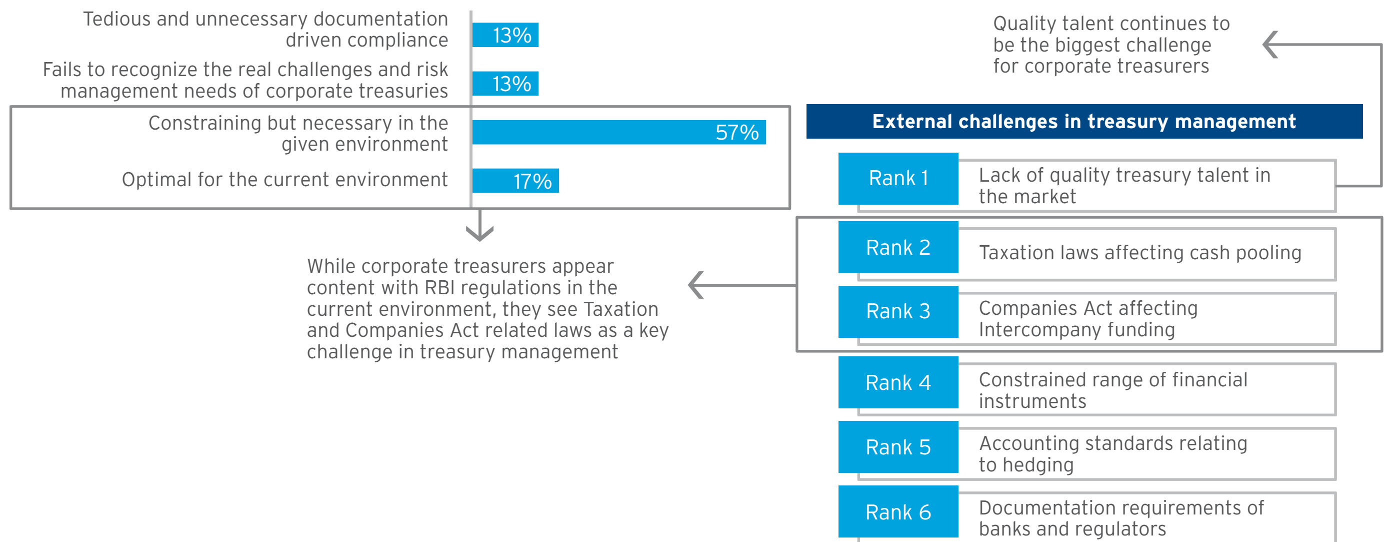
The liquidity management landscape in India has been rapidly evolving. Given the infrastructural challenges to succeed in a highly competitive market like India, it is imperative for corporates to re-evaluate their liquidity management processes and to drive efficiency and automation in treasury management by leveraging new technologies.

Corporates in India should evaluate implementation of multi-bank cash concentration solutions, which allows consolidation of cash positions across multiple banks and gain maximize return on surpluses. These cash concentration solutions enable corporates to gain complete visibility and control of all their account balances, and allows for comprehensive and accurate forecasting and data analytics. Along with automated fund transfers, the administrative burdens to manage fragmented cash positions can now be allocated to other value add areas.

In 2013, changes to the Companies Act made intercompany lending and borrowing cumbersome between group companies. However subsequent amendments in May 2015 have provided some relaxation for private entities to conduct intercompany transactions, thus enabling corporate treasurers to actively start evaluating multi-entity cash concentration structures for optimizing their working capital requirements in India.

Corporate Treasurers Appear at Ease with RBI Regulations but Find Laws Affecting Cash Pooling a Key Business Challenge

Opinion on the Reserve Bank of India ('RBI') regulations for Corporate Treasuries



Source: Deloitte 2015 India Corporate Treasury Survey: Excellence in Corporate Treasury Management

In order to derive maximum value from such cash concentration solutions, it is key for corporates to expand them to multi-entity structures which enable true working capital efficiency, reduction in operating cash and yield enhancement.

Embracing Future Opportunities

As highlighted in the Deloitte survey, the top three priorities for corporate treasurers in India today are: controlling working capital, managing financial risk, and providing and managing liquidity.

Whilst this highlights that these core treasury competencies continue to remain vital, it also draws out the fact that the role of treasury is becoming increasingly strategic, particularly around the areas of managing risk, funding long-term growth and acting as a financial advisor to the business.

With greater understanding of the implications of the aforementioned Taxation and Companies Act related laws as they relate to cash pooling, liquidity management is increasingly transitioning towards centralized treasuries, and thus the use of sweeping and pooling arrangements are gaining in popularity.

To overcome challenges of gaining visibility over cash balances, most organizations initially explore the use of single entity, multi-bank structure, before gradually moving towards multi-entity structures.

The next step on the sophistication ladder of liquidity management is to implement more advanced concepts such as cross border sweeping, notional pooling structures, or re-invoicing centers to centralize settlement and working capital management.

Corporates that are early adopters would succeed.

The liquidity management landscape in India has been rapidly evolving. Given the infrastructural challenges to succeed in a highly competitive market like India, it is imperative for corporates to re-evaluate their liquidity management processes and to drive efficiency and automation in treasury management by leveraging new technologies.

Q&A: Tax Considerations for Companies with Treasury Structures in China

The liberalization of policies in China has created opportunities for many companies to implement treasury structures domestically as well as integrate China into global or regional businesses. In this Q&A dialogue, Kenny Lam from PricewaterhouseCoopers's China Tax Management and Process Services Group addresses commonly-asked questions for businesses with global or regional treasury structures.

Kenny Lam

Tax Partner PRC Tax & Business Advisory Services, PricewaterhouseCoopers (PwC) China

Q1 What are the key tax considerations a corporate should review before implementing a cross-border pooling solution?

A1 For a Chinese entity lending to its overseas affiliates, the Chinese entity would be subject to China corporate income tax of 25% and value-added tax (VAT) of 6% on interest income collected overseas with effect from 1 May 2016. In addition, foreign countries may impose withholding tax on interest income paid to the Chinese entity. In this case, an application for tax credit in China would need to be made with the local Chinese tax authorities. Furthermore, a Chinese stamp duty of 0.005% of the loan amount stated on the contract would be imposed.

For the Chinese entity borrowing from its overseas affiliates, the Chinese entity would be obliged to withhold income tax of 10% and VAT of 6%/(1+6%) on interest income paid to overseas affiliates with effect from May 1, 2016. The same overseas affiliates may also need to apply for tax credit of the withholding income tax of 10% paid in China with their home tax authorities. Similarly, a Chinese stamp duty of 0.005% of the loan amount stated on the contract would be imposed.

Q2 If we select two companies that are affiliates to be involved in the cross-border pool arrangement, would this affect our tax obligations?

A2 The tax implications as stated above would apply in this situation as local Chinese tax authorities expect related parties' transactions to be conducted on an arm's length basis.

Q3 In the case where a Chinese entity borrows from an overseas entity, is the Chinese entity obliged to withhold tax and VAT?

A3 As discussed above, when the Chinese entity pays interest income to its overseas affiliates; it has the obligation to withhold income tax of 10% and VAT of 6%/(1+6%) (effective May 1, 2016).

Q4 Interest income created in cross-border and domestic cash pooling structures is now also subject to VAT. Could you please briefly share how VAT is applied?

A4 From China's tax regulatory perspective, VAT is borne by service recipients in general unless the party responsible for VAT is explicitly defined in the commercial contract. As a brief illustration of VAT under the new VAT regime, a Chinese entity should charge RMB100 interest income plus VAT of 6% to its overseas affiliate. The Chinese entity's interest income would still be RMB100 but the VAT of 6% collected should be available for offset against VAT paid by the Chinese entity to its vendors. Only the net VAT amount needs to be reported by the Chinese entity to the local tax authorities.

Q5 Is VAT applicable on the Entrustment Loan commission collected by the bank as services provided for arranging cash pooling for its customers?

A5 Starting from May 1, 2016, banks in China should issue VAT invoices to customers for this commission and thus customers should be able to claim a VAT credit. However, if a bank provides an overdraft facility to its customers and charges interest, the bank will not issue a VAT invoice. Instead a normal China invoice would be issued, and customers will not be able to claim VAT credit.

Q6 With regards to the new VAT rule of "unified borrowing and unified lending model", is the related interest gain eligible for VAT exemption under a domestic cash pooling structure?

Table: Key Tax Considerations for Chinese Entities

	Chinese entity lending to overseas affiliates	Chinese entity borrowing from overseas affiliates
Corporate income tax	25%	None
Value-added tax (VAT) on interest income	VAT of 6% on interest income collected*	VAT of 6%/(1+6%) on interest income paid*
Withholding tax (WHT)	Foreign countries may impose WHT on interest income paid to Chinese entity	Chinese entity obliged to withhold WHT of 10%, which is imposed on interest payments made to the overseas affiliate
Tax credit application	Application with local Chinese tax authorities if WHT imposed	Overseas affiliate may need to apply with home tax authorities for tax credit on WHT imposed
Stamp duty	0.005% of the loan amount	0.005% of the loan amount

Note: There are no differences between a renminbi (RMB) and foreign currency (FCY) cash pooling solution.

*Effective 1 May 2016, business tax would be replaced by VAT thus only VAT would apply

A6 Interest income arising from entrustment loans between the header company and cash pool participants in the "unified borrowing and unified lending model" of non-bank customers within the same group should be exempted from VAT if the following conditions are met: (1) the header company borrows from financial institutions or issues external corporate bonds, (2) the interest rate charged to the header company is no lower than the interest rate charged to its affiliates. As there are still uncertainties that require further clarification, for example: (1) whether financial institutions include both China and non-China financial institutions, (2) whether external corporate bonds need to be issued within China or include issuance outside of China, please contact your tax consultants for further advice.

Q7 There are differing interest rate benchmarks, between the China onshore (CNY) market and offshore (CNH) markets. Which rate/market best reflects the arms-length nature of the intercompany loan?

A7 China's tax regulation only stipulates that related parties' transactions should be conducted on an arm's length basis. As such, in practice, the local Chinese tax authorities may use the leading rate of similar term announced by the People's Bank of China as a benchmark to assess the reasonableness of the interest rate charged by the Chinese entity or overseas affiliate.

Q8 What considerations would affect the most appropriate benchmark rate?

A8 People's Bank of China's interest rate may be used as a benchmark by the local Chinese tax authorities when assessing the reasonableness of the interest rate charged by the Chinese entity or overseas affiliate.

Q9 In the recent announcement No. 16, 2015 on administrating transfer pricing, how does this affect the borrowing and lending rate to be applied?

A9 Circular16 further strengthens the arm's length principle of related parties' transactions and allows the local Chinese tax authorities to make tax adjustments of up to 10 years. In brief, Circular16 reiterates that outbound payments to overseas related parties should follow the arm's length principle, and that the Chinese payer may be required by local Chinese tax authorities to file relevant documentation with the in-charge tax bureau to support the arm's length basis of the interest rate charged. Additionally, payments to an overseas related party which bear no substantial operation or activities and does not undertake functions or bear risks may not be deductible for China corporate income tax purposes.

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Q&A: Tax Considerations for Companies with Treasury Structures in Hong Kong

The Inland Revenue (Amendment) (No. 2) Ordinance 2016 (Amendment Ordinance), published in the Hong Kong gazette on June 3, 2016, introduces new rules designed to attract foreign companies and companies from Mainland China to establish their corporate treasury centers (CTCs) in Hong Kong to provide centralized treasury management services to companies in their groups.

Samantha Tan
Tax Senior Manager,
International and M&A
Tax Services,
Deloitte Touche Tohmatsu

Samantha Tan, Tax Senior Manager, International and M&A Tax Services with Deloitte Touche Tohmatsu in Hong Kong, answers some frequently asked questions on the new Hong Kong CTC regime.

Q1 What are the key features of the Hong Kong CTC regime?

A1 The Amendment Ordinance prescribes amendments to the Inland Revenue Ordinance (IRO) to allow for qualifying CTCs to be taxed at a concessionary Hong Kong profits tax (HKPT) rate of 8.25% on profits derived from qualifying lending transactions, corporate treasury services and corporate treasury transactions conducted with or in connection with a non-Hong Kong associated corporation. The current interest deduction rules under the IRO would also be amended to allow certain Hong Kong corporations (not only qualifying CTCs) deductions on interest paid to foreign associated corporations, subject to conditions being met.

Q2 How can corporations qualify as a "qualifying CTC"? What is the application process?

A2 In order to be a qualifying CTC, a corporation's central management and control should be exercised in Hong Kong, and it must not be a financial institution as defined under the IRO. A corporation that carries on only corporate treasury activities and non-income generating activities may qualify as a "dedicated CTC". A corporation that also carries on both corporate treasury activities and non-corporate treasury

activities that generate income, such as trading or manufacturing, would also qualify as a "multi-function CTC", if it meets a certain "profits test" and an "asset test". Lastly, a CTC that does not meet the criteria of either a dedicated CTC or a multi-function CTC may also obtain a determination from the Commissioner of Inland Revenue (CIR).

As regards application procedures, there would not seem to be any prescribed under the Amendment Ordinance, apart from the requirement that the corporation would have to make an election to be chargeable to HKPT at the concessionary rate as a qualifying CTC. Once made, such an election would be irrevocable for so long as the corporation remains a qualifying CTC. As of the date of writing, the Inland Revenue Department has not issued any guidance on the procedures that a corporation should follow to obtain the CIR's determination or undertake a self-election.

Q3 What if I am already a corporation carrying on a sales and trading business in Hong Kong, and I already perform certain treasury activities? Can I still benefit from the Hong Kong CTC regime?

A3 A corporation that already carries on sales and trading activities and corporate treasury activities in Hong Kong could elect to be a qualifying CTC. Given the nature of its business, it may potentially qualify as a multi-function CTC (question 2 refers) if it meets the "profits test" and "assets test" in that particular year of assessment (subject year). Essentially, this means that its corporate treasury profits and corporate treasury assets of the corporation should constitute 75% or more of its total profits and assets for that year.

Alternatively, the corporation could also qualify as a multi-function CTC in the subject year if its average corporate treasury profit percentage and average corporate treasury asset percentage are 75% or morefor a safe harbor period of either 2 or 3 years. The number of years considered in calculating the average percentages depends on how long the corporation has been carrying on a business in Hong Kong prior to the year in which it is determining its CTC status.

Q4 Is the Hong Kong CTC regime right for your organization?

Whether your organization could benefit from the Hong Kong CTC regime depends on its commercial and operational needs. One pertinent issue to consider is whether another entity should be established to act as a dedicated CTC, or if your organization could undertake corporate treasury activities alongside other revenue-generating activities as a multi-function CTC.

If your organization seeks to qualify as a multi-function CTC, it may not be easy for it to fulfill the "profits test" and "asset test"; for instance, if you are a sales and trading company that may only perform corporate treasury activities as a secondary function in support of the main functions of sales and trading, you might find that your trading profits would generally surpass income from, say, the spread of borrowing and lending interest rates from financing activities.

The other factor would be whether your organization should set up a CTC in Hong Kong or in another location that offer tax incentives for CTCs in the Asia Pacific region, such as Singapore, Thailand or Malaysia. The availability of tax incentives in each of these jurisdictions is generally subject to criteria tied to local spending, creation of local employment, etc. While the Hong Kong CTC regime has comparatively fewer conditions on employee headcount and annual expenditure, whether it should be the location of choice will ultimately depend on your operational needs and resources.

All in all, whether your organization should set up a Hong Kong CTC, and if so, the form that it should take, should be analyzed on a case-by-case basis.

Q5 What are the requirements to segregate and report to Inland Revenue Department (IRD) with regards to the profits test and asset test?

A5 There is no guidance on the practical aspects of the Hong Kong CTC regime from the IRD as yet. However, it would be likely that a corporation looking to establish its CTC status for a subject year would probably need to submit a statement of its corporate treasury profits and corporate treasury assets together with its Profits Tax Return during the year, and show a calculation of the corporate treasury profit and corporate treasury asset percentages for that year. If the multi-year safe harbor is relied on, the same information may need to be submitted for the safe harbor period of either 2 or 3 years.

Q6 What are the tax considerations for a Hong Kong CTC acting as a global cash concentration header?

A6 In the post-BEPS era, a Hong Kong CTC should have sufficient business substance to qualify for tax concession under the Hong Kong CTC regime and to enjoy double tax treaty benefits (e.g. preferential interest withholding tax rates on interest income from pool participants). A certain level of business substance in Hong Kong would therefore be necessary; for instance the Hong Kong CTC should have an office, directors and personnel in Hong Kong.

Increased transfer pricing and reporting requirements under BEPS may mean that tax authorities of the jurisdictions covered by the cash pool structure may require comprehensive information on the cash pooling arrangements, financial information of the Hong Kong CTC and other pool participants, details of transfer pricing policies, transactions and documentation. A transfer pricing study should be undertaken in respect of the cash pooling structure and supported by contemporaneous transfer pricing documentation.

Q7 What are the tax considerations for a Hong Kong CTC that acts as a re-invoicing center or in-house bank conducting payment-on-behalf-of (POBO) activities?

A7 Similar to a Hong Kong CTC that acts as a global cash concentration header (as discussed in question 6), a Hong Kong CTC that undertakes re-invoicing or POBO activities for group companies should also have sufficient business substance to qualify for tax concession under the Hong Kong CTC regime and to enjoy double tax treaty benefits. It may also be subject to increased transfer pricing and reporting requirements; again, transfer pricing analysis as supported by proper contemporaneous documentation is important.

Depending on the extent of the Hong Kong CTC's presence and operations in the jurisdictions of the group companies for whom it undertakes POBO, it may need to consider whether its operations would create permanent establishment (PE) issues in those jurisdictions. Similarly, it should be considered as to whether the group companies to whom the Hong Kong CTC provides re-invoicing or POBO services in Hong Kong would have a taxable presence in Hong Kong due to the Hong Kong CTC's activities.

Q8 What is the expected implementation date?

A8 The CTC rules and interest deductibility rules should take effect retrospectively from April 1, 2016.

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Q&A: Market Perspectives on Corporate Treasury Centers in Hong Kong

Growth in Asia can be understood in binary terms: first through global multinational corporations (MNCs) continuing to develop business in the region and second through Asia-based corporations expanding outside their home markets in Asia. These companies are now looking to establish corporate treasury centers (CTCs) in the region to support treasury centralization initiatives to enhance efficiency and improve visibility.

Enoch Fung

Head (Market Development), External Department, Hong Kong Monetary Authority

Howard Yang

Head of Treasury and Trade Solutions, Hong Kong, Citi

In May 2016, the Hong Kong Legislative Council passed an Amendment Bill to the Inland Revenue Ordinance to introduce new rules designed to attract foreign companies and companies from Mainland China to establish their CTCs in Hong Kong. In this feature, **Enoch Fung**, Head (Market Development) at Hong Kong Monetary Authority (HKMA) and **Howard Yang**, Head of Treasury and Trade Solutions at Citi Hong Kong discuss with **Ann Lin Khoo**, Head, Market Management, Liquidity Structures, Asia Pacific, Treasury and Trade Solutions at Citi on what these new rules mean for corporates looking to establish a treasury center in Hong Kong.

Q1 Ann Lin Khoo: What were the reasons behind the introduction of the new CTC initiative in Hong Kong?

A1 **Enoch Fung:** We noticed an increasing number of MNCs expanding their business in Asia to capture stronger economic growth in the region. Meanwhile, we also noticed Mainland China corporations boosting their overseas investments under the "Going Out" policy of the Chinese Government.

Being an international finance center with a solid foundation, Hong Kong is naturally primed to support corporates in all kinds of corporate treasury activities. We anticipate the new CTC rules to add to Hong Kong's existing advantages to be a regional and global hub for CTCs. We look forward to more CTCs being set up in Hong Kong to bring more flows and activities to our financial and professional industries.

Q2 Ann Lin: What are the key changes introduced in the Inland Revenue Bill?

A2 **Enoch:** The changes introduced in the Inland Revenue (Amendment) (No. 2) Ordinance 2016 are as follow:

a Interest deduction rules have been adjusted to allow a corporate borrower carrying on in Hong Kong an intra-group financing business deduction of interest payable on money borrowed from a non-Hong Kong associated corporation under specified conditions

b Provides for a regime under the IRO in which the tax rate on qualifying profits of a qualifying CTC derived from qualifying corporate treasury activities is 50% of the prevailing profits tax rate for corporations (i.e. 16.5% x 50% = 8.25%)

Under the half-rate regime,

- A qualifying CTC should be a standalone corporate entity with 75% or above of its profits and assets related to qualifying corporate treasury activities
- The list of qualifying corporate treasury activities is prescribed in the law and encompasses a wide range of services or transactions including cash pooling, liquidity management, payment processing, corporate finance and risk management
- The concessionary tax rate can be elected through tax filing without separate application or approval process

Q3 Ann Lin: How does Hong Kong compare to other locations in the Asia Pacific region in supporting corporates with their treasury center activities?

A3 **Howard Yang:** Hong Kong has always been a good location for corporates centralizing their treasury management activities in the region, even without a formal incentive program as introduced in Singapore, Thailand and Malaysia. Now, with the introduction of the CTC regime, along with Hong Kong's stable infrastructure including an efficient clearing infrastructure, treasury talent fluent in English, Chinese (Mandarin) and Chinese(Cantonese), there is a strong foundation to support corporates in facilitating their international payments and collections, intra-group funding, liquidity and risk management activities.

Q4 Ann Lin: Which corporate profiles would benefit the most from establishing a CTC in Hong Kong?

A4 **Howard:** Generally, companies with significant business presence in the Greater China region would benefit the most from establishing Hong Kong as a treasury location. This is largely due to the close proximity, double taxation agreement with Mainland China and language similarities.

Q5 Ann Lin: Why should companies choose Hong Kong as a leading location for treasury management activities?

A5 **Enoch**: Hong Kong is a leading international financial and commercial center in Asia. With a number of key strengths, we believe Hong Kong is an attractive location for corporates to centralize their CTC activities. Hong Kong's strengths include:

a **Robust bank platform and deep financial markets**
Around 70 of the world's 100 largest banks have a presence in Hong Kong. We also have one of the most active equity and debt markets in the world

b **Largest offshore RMB center in the world**
Hong Kong is the largest offshore RMB liquidity pool with around RMB800 billion of deposits. Today, over 70% of RMB payments by value in SWIFT go through Hong Kong. Hong Kong has an active foreign exchange and rates market with liquidity support from the HKMA to the market (as of May 2016)

c **Key hub of commercial activities**
Hong Kong is a regional hub for commercial activities with over 7,900 regional headquarters, regional offices and representative offices

d **Close proximity to China**
In 2014, from a cross-border investment standpoint, around 58% of China's outward direct investment (ODI) and 68% of China's foreign direct investment (FDI) were made through Hong Kong, reflecting Hong Kong's pivotal role as a springboard for China's cross-border investment flows

e **Free flow of capital**
Free flow of capital is protected by the basic law, the de facto constitution of Hong Kong

f **Convenient hub in Asia**
Hong Kong is located in the heart of Asia, with half of the world's population reachable within five hours of flight

g **Favorable tax environment**
Hong Kong has one of the simplest tax regimes among Asia countries. The CTC regime allows a competitive concessionary tax rate to qualifying CTCs for their CTC activities. Hong Kong has the most favorable double tax agreement with Mainland China, with a withholding tax rate of 7% on interest payments from the Mainland. In addition, the government has been working hard to expand the double taxation agreement network to more countries, from 5 in 2009 to 35 in May 2016.

A5 **Howard**: From Citi's experience, deciding on a corporate treasury location is never a simple exercise as it depends on company/legal entity structures, treasury personnel, business model, etc. Generally, I would say that companies with significant business presence in the Greater China region would benefit the most from using Hong Kong as a treasury location on the basis of culture/language commonality, proximity and more favorable tax considerations as Enoch has mentioned.

Q6 Ann Lin: Lastly, what further advice would you offer to corporates looking to select Hong Kong as a treasury management location?

A6 **Enoch**: Be forward looking. The CTC set up can be seen as a financial engine to support new growth areas for corporates. Corporates may seek to align the location of the CTC with the areas where they find most growth opportunities, and require most funding support.

Corporates may seek professional tax planning services for a comprehensive study of the tax implications to the operations of setting up CTCs in different locations. The implications of a CTC tax regime can vary to corporates with different operating models.

A6 **Howard**: While tax is an important element, there are many other considerations like solid accounting policies and legal entity structures that should be considered. Particular key points corporates should deliberate are:

a Initiatives to attract and retain treasury talent to manage the Hong Kong CTC in the long term

b Enable flexibility – apply consistencies with global policies yet allowing quick responses in managing intricacies of the Greater China environment

c Partner with a global bank like Citi who understands the intricacies of enabling flexibility while ensuring global practice consistencies

Hong Kong is a leading international financial and commercial center in Asia. With a number of key strengths, we believe Hong Kong is an attractive location for corporates to centralize their CTC activities.

Q&A: Tax Considerations for Companies with Treasury Structures in Singapore

Across Asia, the competition to attract companies to establish a corporate treasury center between locations has strengthened. Last year, the Hong Kong government introduced new rules designed to attract foreign and Mainland China companies to the city. This year, Singapore introduced enhancements to its Finance and Treasury Centre (FTC) scheme. Announced during the Singapore Budget 2016, the Singapore FTC Scheme has been extended to March 31, 2021, with major changes effective March 25, 2016.

Michael Velten
Tax Partner and Financial Services Tax Leader,
Deloitte & Touche LLP

In this Q&A feature, **Michael Velten**, Tax Partner and Financial Services Tax Leader at Deloitte & Touche LLP answers some frequently asked questions on the scheme.

Q1 What are the different tax initiatives available for companies using Singapore as a corporate treasury location?

A1 Singapore offers many tax incentives in a wide range of industries. Generally, the enhanced FTC incentive would provide a tax concession of 8% on qualifying profits from qualifying treasury activities if corporate treasury activities are conducted in Singapore.

If a multinational company plans to base its international headquarters in Singapore, a concessionary tax rate of as low as 5% on incremental income from qualifying activities, which could include corporate treasury activities, may be granted. The concessionary rate of tax and/or tenure of these incentives will vary depending on the level of economic resources committed by the taxpayer to Singapore.

Q2 What are the features of the FTC incentive prior to the enhancements announced on March 25, 2016 during the Singapore Budget 2016? What are the enhancements to the FTC incentive?

A2 Prior to the Singapore Budget 2016, the FTC incentive provided a reduced corporate tax rate of 10% on fees, interest and gains derived by a FTC from conducting qualifying activities on its own account or providing qualifying services to its offices and network companies (ANCs). Loan interest paid by the FTC to overseas banks and ANCs was also exempt from Singapore interest withholding tax, provided that the funds must be used by the FTC for the conduct of qualifying activities or services. The funds used by the approved FTC for carrying out the activities were required to be obtained directly from qualifying sources.

The Singapore Budget 2016, delivered on March 25, 2016, proposed a number of enhancements to the FTC incentive; in addition to extending the incentive beyond its then sunset date of March 31, 2016. The concessionary tax rate on qualifying income was reduced to 8% from 10%, withholding tax exemption is extended to interest payments on deposits placed with the FTC by overseas ANCs (provided that the funds are used by the FTC for the conduct of qualifying activities or services) and the FTC will be allowed to obtain funds both directly and indirectly from ANCs, subject to meeting certain anti-avoidance conditions. The enhanced FTC incentive has a sunset date of March 31, 2021.

Q3 What are the key qualifying criteria(s) for the FTC incentive after March 31, 2016?

A3 The Singapore Economic Development Board (EDB) issued a Circular on June 1, 2016, which provides further details on the enhanced FTC incentive.

While the Circular indicates that there will be increased substantive requirements for new FTC applicants and FTC renewal cases, specific guidance on the qualifying criteria was not provided. Previously, the minimum requirements were that the FTC should incur annual business expenditure of SGD750,000, hire a minimum of three professionals based in Singapore and who are engaged substantially in the FTC's qualifying activities and services, and provide at least three qualifying activities to three or more network companies.

It is believed that these substantive requirements should still be met as a minimum, but EDB is likely to require additional commitments from new FTC applicants and renewal cases going forward. Also, EDB may focus more on the quality of services performed in Singapore rather than the quantity. In any case, each new or renewal application will be subject to approval on a case-by-case basis by the EDB.

It is believed that these substantive requirements should still be met as a minimum, but EDB is likely to require additional commitments from new FTC applicants and renewal cases going forward. Also, EDB may focus more on the quality of services performed in Singapore rather than the quantity.

Q4 What is the application process for new applicants to the FTC incentive?

A4 After assessing the applicant's company's business case to ascertain whether the minimum qualifying criteria of the EDB are met, the applicant may then have a preliminary meeting with the EDB to present their broad business plans and strategies. This will be followed by a formal application for the FTC incentive by completing and submitting the prescribed application form to be obtained from the EDB, together with qualitative and quantitative information relating to the applicant's business plans.

After EDB reviews the application form and documents submitted, there will usually be a follow up meeting between the applicant and EDB to discuss (and potentially negotiate) the terms and conditions for the FTC incentive.

Once the terms of the FTC incentive have been agreed between the applicant and the EDB in principle, an offer letter will be issued to the company, which sets out the terms of the tax incentive and the conditions to be met. The FTC incentive is generally granted on a five year basis.

Q5 What if a company is already enjoying the benefits of the FTC regime approved before March 31, 2016? How can the company enjoy the benefits under the enhanced FTC incentive?

A5 The company may be able to apply for an early renewal of the FTC. If approved by the EDB, the process would be similar to that outlined for new applicants above. The company should generally expect to commit a higher level of financial and manpower resources in Singapore.

After assessing the applicant's company's business case to ascertain whether the minimum qualifying criteria of the EDB are met, the applicant may then have a preliminary meeting with the EDB to present their broad business plans and strategies.

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Q&A: Market Perspectives on Singapore's Finance and Treasury Centre Scheme

In June 2016, the Singapore government released enhanced rules to the Finance and Treasury Centre (FTC) Scheme, extending the FTC scheme for qualifying companies to March 31, 2021. As growth in Asia arise from global multinational corporations (MNCs) developing business in the region and home-grown corporations expanding outside their local countries, companies are looking to establish treasury centers in the region to support treasury initiatives to increase efficiency and improve visibility.

Anita Loh
Head of Product Management, Singapore, Treasury and Trade Solutions, Citi

Bernard Wee
Executive Director, Financial Markets Development, Monetary Authority of Singapore

In this feature, **Bernard Wee**, Executive Director, Financial Markets Development, Monetary Authority of Singapore (MAS) and **Anita Loh**, Head of Product Management, Singapore, Treasury and Trade Solutions, Citi discuss with **Nishami Dharmaratne**, Head, Multinational Corporates, Liquidity Management Services, Asia Pacific, Treasury and Trade Solutions at Citi on what these new rules mean for corporates looking to establish a treasury center in Singapore.

Q1 Nishami Dharmaratne: What were the reasons behind the enhancements introduced in the FTC scheme?

A1 **Bernard Wee**: Asia remains the key driver of the global economy, and MNCs, including from within Asia, continue to expand their businesses in the region. Singapore was a pioneer in helping multinationals manage an efficient treasury footprint. In order to stay ahead, we consulted, we listened, and we decided to enhance the FTC scheme to strengthen Singapore's attractiveness as a treasury center.

Q2 Nishami: What are the key enhancements which have been introduced in the Singapore Budget 2016?

A2 **Bernard**: The enhancements are threefold:

- The concessionary tax rate has been lowered from 10% to 8%, with corresponding increase in three substantive requirements;
- Under the enhanced scheme, FTCs are now allowed to obtain funds indirectly from approved offices and associated companies with adequate safeguards against round-tripping; and
- The scope of the tax exemption has been expanded to cover interest payments on deposits placed with the FTC by its non-resident approved offices and associated companies, provided the funds are used for the conduct of qualifying activities or services.

The enhanced FTC scheme is extended until March 2021. Successful applicants can enjoy the benefits of the scheme for five years, subject to renewal thereafter.

Q3 Nishami: How does Singapore compare to other locations in the Asia Pacific region in supporting corporates with their treasury center activities?

A3 **Anita Loh**: With an experienced talent pool and stable infrastructure, and legal framework there is no doubt that Singapore holds the leading position for corporates to centralize their cash and treasury management activities in Asia.

Bernard: Singapore is one of the most attractive jurisdictions to start and run a business. The World Bank has named Singapore the world's easiest place to do business for 11 consecutive years (up till 2016). Singapore has also risen to third spot in the Global Financial Centre Index, after London and New York in a survey published in April 2016. Companies based in Singapore can benefit from our broad network of 20 Free Trade Agreements and 80 Avoidance of Double Taxation Agreements.

Singapore's key strength lies in a deep and trusted financial market backed by a strong legal framework Companies are able to access a myriad of capital raising opportunities and a wide range of sophisticated risk management products through our network of global and regional financial institutions and exchanges.

Q4 Nishami: Which corporate profiles would benefit the most from establishing a FTC in Singapore?

A4 **Anita**: Generally companies with business presence across the Asia region, particularly in the ASEAN framework would benefit the most in establishing Singapore as a treasury location. This is largely due to the close proximity, expansive double taxation agreement (DTA) network and experienced treasury center talent pool.

Bernard: Singapore's key strength lies in a deep and trusted financial market backed by a strong legal framework. Companies are able to access a myriad of capital raising opportunities and a wide range of sophisticated risk management products through our network of global and regional financial institutions and exchanges. Companies with considerable business interests across multiple markets would benefit from setting up an FTC in Singapore in order to access a comprehensive suite of products and services for their diverse needs.

From our experience, there are companies from a broad range of industries from consumer electronics to manufacturing, IT, automobile and commodity trading firms that have chosen Singapore as a regional business and FTC hub. They have not only set up their regional corporate treasury centers in Singapore, but also their regional HQ and R&D functions here, to leverage on Singapore's connectivity into the region and excellent infrastructure.

Q5 Nishami: Why should companies choose Singapore as a leading location for treasury management activities?

A5 **Bernard**: Since the 90s, Singapore has grown to be the banking and treasury hub of the region, and is now world's number 3 financial center after London and New York. We have attracted a strong network of APAC transactional banking teams from global and regional banks in Singapore, capable of serving a treasurer's cash management and complex risk management needs. As the third largest FX center globally, Singapore's average daily trading volume grew 26% from October 2015 to reach USD507 billion April 2016, according to the Singapore FX Market Committee survey. Singapore offers corporates with ready access to effective hedging solutions through the most liquid FX market in Asia. Some sophisticated corporate treasurers in Singapore have even set up centralized FX dealing desk to provide FX solutions to their network companies.

Singapore also offers companies effective channels to manage cross-border financial flows between Singapore and key markets in the region. Building on Singapore's strength as an offshore RMB hub, China and Singapore introduced a pilot scheme for cross-border RMB transactions which allows companies in Suzhou, Tianjin and Chongqing to issue RMB bonds or borrow RMB from banks in Singapore and repatriate the proceeds to China. Singapore is also geographically well positioned to serve India. Indian companies are already tapping Singapore's capital market in a significant way through company and business trust listings, and close to 80% of international Indian bond issues are listed on the SGX. With the deep pool of institutional investors in Singapore, companies can readily raise debt from a diversified investor base.

Beyond financial services, Singapore serves as a well-connected center with extensive commercial and transportation links into ASEAN, China and India, thereby allowing the FTC to enjoy the 'best of both worlds'.

Anita: From Citi's experience, deciding on a corporate treasury location is never a simple exercise as it depends on company/legal entity structures, treasury personnel, business model, etc. In a 2015 Global Corporate Treasury Survey issued by Deloitte in January 2015 (updated June 2015), corporates state the increasing importance for corporate treasurers to continue to manage liquidity risk and be a strategic advisor to the business and be able to access the capital market as and when to finance growth. Bearing on these traits, it is important for a treasury center to be located in a center like Singapore which enables these critical considerations as well as enable access to an experienced talent pool to manage complex treasury activities.

Q6 Nishami: Lastly, what further advice would you offer to corporates looking to select Singapore as a treasury management location?

A6 **Bernard**: Talent is critical to the success of any venture and companies should consider places where it is easy and attractive to find and place talent. There is also a wide selection of international schools for the employees' family and Singapore offers a good quality of life.

Singapore is where East meets West. We are a vibrant and cosmopolitan city and have been ranked consistently as the top destination in Asia by expatriates. With this combination of lifestyle, business, finance, and talent factors, we hope we offer a compelling value proposition for companies to consider Singapore as their regional or global corporate treasury hub.

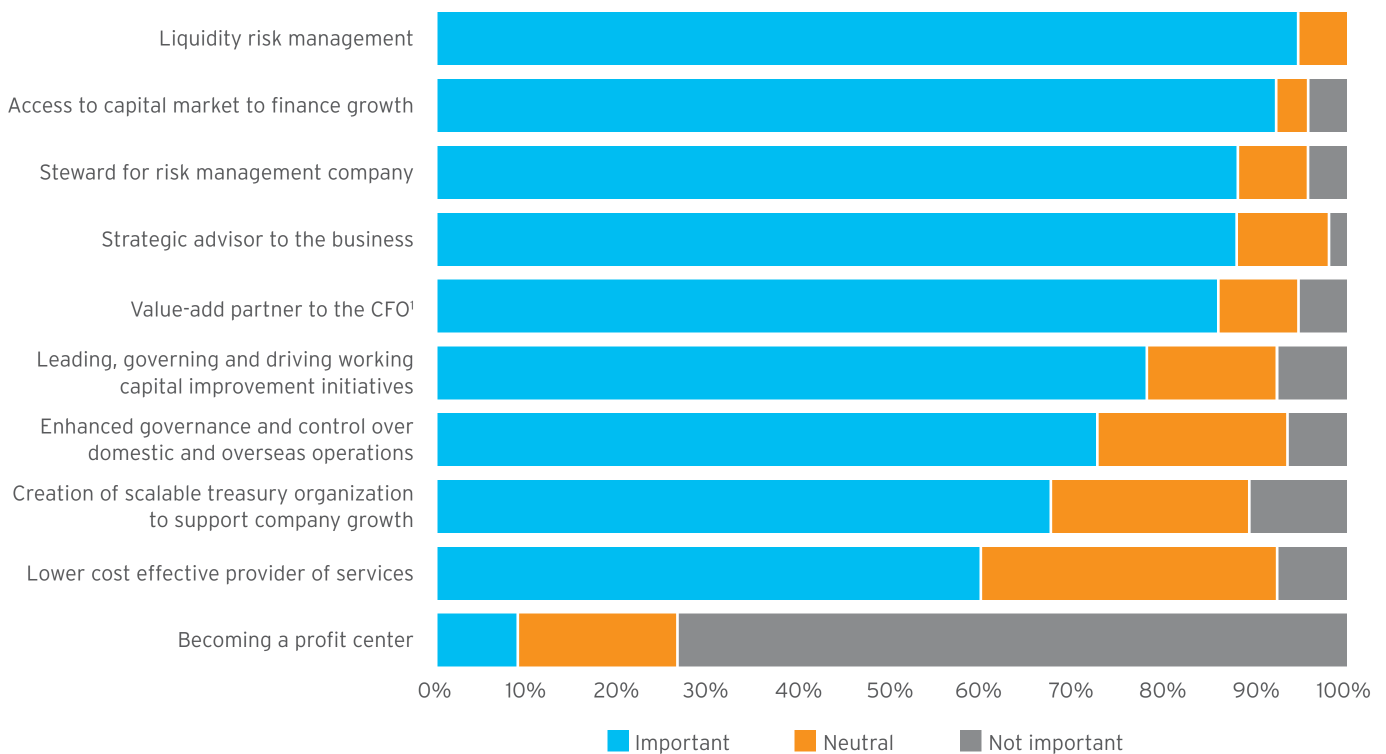
Anita: While tax is an important element, there are many other considerations like solid accounting policies and legal entity structures that should be considered. Particular key points corporates should deliberate are:

a Access to an experienced talent pool

b Ease of FX conversion/cross-border transactions

c Political and regulations stability

d Partner with a global bank who understands the intricacies of enabling flexibility while ensuring global practice consistencies



[1] e.g., support or drive M&A activity.

Source: 2015 Global Corporate Treasury Survey, Deloitte

With this combination of lifestyle, business, finance, and talent factors, we hope we offer a compelling value proposition for companies to consider Singapore as their regional or global corporate treasury hub.

Q&A: Tax Considerations for Companies with Treasury Structures in Thailand

Across Asia, the competition to attract companies to set up a corporate treasury center has stiffened of late. Several locations have recently enacted various policies and enhancements to draw both multinational and home-grown companies alike to their shores.

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In this feature, **Poljun Divari**, Legal Director and **Niorn Yukolthong**, Tax Manager at Deloitte Touche Tohmatsu Jaiyos Advisory answer some frequently asked questions on the current Bank of Thailand scheme, which provides further incentives to establish their treasury centers in Thailand, in addition to being a centralized location for trading and investment operations in ASEAN.

Q1 What are the key tax benefits of carrying out borrowing and lending activities and/ or other corporate treasury activities through a treasury center?

A1 The key tax benefits of a treasury center applied under the International Headquarters ("IHQ") regime include:

- A 15-accounting periods corporate income tax ("CIT") exemption on qualifying treasury center services provided to foreign associated enterprises and capital gains on transfer of shares in a foreign associated enterprise.
- A 15-accounting periods 10% CIT (reduced from the current standard 20% rate) on qualifying treasury center services provided to Thai associated enterprises.
- A withholding tax ("WHT") exemption on dividends (from exempt profits) distributed by the IHQ to its foreign corporate shareholders that do not carry on business in Thailand.
- A WHT exemption on interest paid by the IHQ to foreign corporate lender on loans acquired for re-lending to associated enterprises in the context of treasury center services.
- Specific business tax exemption on income derived by the IHQ from provision of qualified financial management services to associated enterprises.
- A 15% reduced personal income tax rate on employment income of expatriates who work for IHQ.

Q2 What are the resources that clients need to establish a treasury center?

A2 Treasury center license procedures

The application for establishment of a treasury center should be submitted to the Bank of Thailand ("BOT") together with supporting documentation. The BOT will review the application as well as supporting documentation, before proposing to the Ministry of Finance to approve and issue a treasury center licence.

A foreign business license issued by the Ministry of Commerce ("MOC") is required if the applicant is defined as a foreign juristic person under the Foreign Business Act B.E. 2542 (A.D. 1999). Also, prior to conducting treasury center business, the treasury center must amend/add the scope of treasury center business in the objectives of the company with the MOC. Once completed, the treasury center has to provide evidence of amendments/additions to the company's objective to the BOT.

The conditions for an applicant to qualify as a treasury center are briefly summarized below:

i A company registered in Thailand; whether established solely for the purpose of operating under a treasury center license, or a pre-existing operating company.

ii A company operating as a treasury center and its group companies shall be affiliated companies.

iii Managing foreign exchange for group companies that have the following qualifications:

- Three group companies in Thailand, Vietnam and neighboring countries; or
- Two group companies in Thailand, or two affiliated companies in other countries

iv The group companies must be engaged in international trade/services and not be engaged in financial services.

Relaxation may be granted and approved on a case-by-case basis subject to the sole discretion of the competent authority i.e. the BOT officer.

Treasury center under IHQ regime

If the treasury center wishes to apply for tax incentives under the IHQ regime, it is required to file an online application on the Thai Revenue Department's website and complete the online information requests, for example, business plan/analysis, company background, treasury center license, 3-year operation plan, 3-year income/expense forecast, etc.

Non-tax incentives are made available by the Thailand Board of Investment ("BOI") and are subject to certain conditions. Some examples of the incentives available are permission to bring in skilled personnel and experts into Thailand, permission to own land, etc.

Q3 If the company were to establish a treasury center, should they establish that as a separated department or as a new entity?

A3 This would depend upon various factors, for example, human resources, physical location, cost efficiency, etc. Certain companies choose to set up the treasury center to operate as a standalone in a new entity in order to minimize the complications that would otherwise be involved with separating the treasury center business operations from other normal business operations.

Q4 If the treasury center is also the IHQ for the group in Asia Pacific, and it borrows funds from financial institutions offshore or group companies offshore, are there any withholding tax consequences?

A4 WHT is exempt on interest paid by the IHQ pertaining to loans acquired by the treasury center from a foreign company that is not carrying on business in Thailand for on-lending to associated enterprises in the context of the treasury center providing financial management services.

Q5 What if that establishment of treasury center does not happen right after the company earns a treasury center license, what are the consequences?

A5 A treasury center license has a duration of one year and is extended one year at a time. However, if there is any suspicion or any reason to believe that the treasury center is failing to comply with or is violating the exchange control law, regulations or notifications or any other matters deemed as inappropriate, the BOT officer may revoke, or not renew the treasury center license. In addition, if a substantial amount of time has passed since an approval to establish a treasury center was obtained, but no transactions have yet taken place, then the BOT may request a clarification letter from the company as to why.

The BOT officer may, at his/her discretion, present to the Ministry of Finance the proposal to revoke, or not to renew the license if he/she sees any non-compliance action or any other issues deemed as inappropriate by the treasury center.

Q6 If the treasury center is also an IHQ as a separated department in the same company, what would the tax reporting process and requirements be?

A6 The income and expense of the treasury center [IHQ] business is to be separated from other businesses that are being carried on. Any expense that cannot be clearly classified as that of any specific business should be in proportion to the income of the qualified treasury center [IHQ] business and other businesses.

Additionally, the computation of the treasury center [IHQ] income that qualifies for the tax exemption should be separately calculated from treasury center [IHQ] income that qualifies for the tax-reduction. Any expense that cannot be clearly separated should be apportioned proportionally to both income qualifying for the tax-exemption and income qualifying for the tax-reduction.

Q7 Why is the company restricted from getting loans from financial institutions or group companies by issuing bonds? Will there be any relaxation on this afterwards?

A7 The BOT recently provided some relaxations. Treasury centers may issue foreign-denominated financial instruments issued in domestic and foreign countries to raise money and invest in foreign-denominated securities issued in foreign countries. In such case, treasury centers shall obtain prior approval from the officer of the BOT.

In order to buy or exchange foreign currency with an authorized juristic person for investing in foreign-denominated financial instruments in foreign countries or those issued and sold in Thailand, the treasury centers shall buy or exchange in the total of not exceeding USD500 million or its equivalent at the market rate per year.

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BASF

In SAFE Hands – Liquidity, POBO/COBO and Netting Solution in China

Headquartered in Ludwigshafen, Germany, BASF is a world leading chemical company combining economic success with environmental protection and social responsibility. China is the multinational's third-largest market worldwide.

The Challenge

BASF's 44 majority-owned subsidiaries in China did not have a centralised foreign currency liquidity management structure. As such, some entities relied on bank loans to fund working capital needs, while others sat on idle US dollars that had limited investment channels.

Since BASF's liquidity in China was isolated from its global liquidity structure, it came with a few drawbacks including costly onshore external funding that is significantly higher than the offshore funding rates. As such, limited intercompany borrowings were conducted under China's foreign-debt borrowing framework, which required case-by-case regulatory approvals and manual efforts. The inefficient process thus consumed significant time of BASF's treasury department.

The Solution

The multinational was nominated by SAFE's Head Office to participate in China's Nationwide Pilot Programme for foreign currency cross-border pooling, POBO/COBO and netting. BASF was the first company in China with approval to pilot a comprehensive solution including:

- Domestic and cross-border USD cash pool to centralize foreign currency liquidity.
- Payment-on-behalf-of/collections-on-behalf-of (POBO/COBO).
- Netting for cross-border settlement with cross-bank foreign exchange (FX) conversion.
- Conversion of Chinese Yuan (CNY) to foreign currency (FCY). FCY payments can also be processed separately by different banks.

Supported by Citi through the pilot, the conglomerate has benefited from access to cheaper offshore funding and reduced its reliance on onshore bank loans for working capital needs. Under the pooling arrangement, BASF (China) Company Limited serves as the pool header for the automatic, end-of-day sweep involving 24 domestic entities in China and two overseas entities in Belgium and Germany.

When China is cash-rich, the sweep is made from China to BASF Head Office's account located in New York. When China is short of cash, funds will first be swept from the non-resident account of BASF Belgium Coordination Centre (BASF's finance hub in Europe) located in China. If that is insufficient, funds will then be swept from BASF SE's account in New York to cover the funding shortage in China.

The Result

The market-first solution is tailor-made to address BASF's specific treasury management needs and has achieved an optimal cash management structure. Deploying cutting-edge technology on an automated online platform and system, the solution is capable of implementing complex projects. This solution also secured China's regulatory approval quickly, which was not available to other companies at the time and has not only transformed BASF's treasury management in China, but is expected to be emulated by other companies seeking similar benefits.

Key benefits included:

- An optimal liquidity management structure which scores high on visibility, mobilization and optimization.
- Lower funding costs and reduced bank fees and transactional charges.
- Fully automated STP for liquidity management, payments, collections and reconciliation.
- Netting of cross-border intercompany transactions has reduced the amount of FX conversion, thus cutting down the trading costs.
- Enhanced risk management measures.

"Through the fully automated, cross-border cash pooling, BASF's global cash mobility and visibility has been greatly enhanced." Moreover, the issue of high onshore external funding costs is resolved since cash is no longer left idle in China, and the offshore centres are allowed to fund domestic working capital needs in a 'just in time' and automated manner. Substantial and tangible savings on funding costs and transaction costs and efficiency gains were achieved as well.

– Sharon Wang, Senior Manager, Treasury Asia Pacific, BASF

A version of this case study was first published in Treasury Today Asia: Adam Smith Asia Awards 2015

HINDUSTAN UNILEVER LIMITED

Best-in-Class Bank Account Rationalization, Simplification and Automation

Hindustan Unilever Limited (HUL) is India's largest FMCG company. A subsidiary of Unilever, the company has a product portfolio that spans across soaps and detergents, personal care products, foods and beverages. It is listed on the Bombay Stock Exchange and National Stock Exchange in India.

The Challenge

HUL's treasury team was looking to simplify banking operations to support the growth and future needs of their business across an extensive value chain footprint whilst 'doing more with less'. Recognizing the context of a fast growing business and an evolving environment, HUL embarked on a journey to transform their transactional banking capabilities, with a view of making it future ready by strongly emphasizing on automation and simplification.

The Solution

Partnering with Citi, HUL implemented an integrated cash management structure with the following key components:

- SWIFT ISO based payment instructions for all types of payments including statutory taxes and levies directly integrated with SAP
- Supplier finance/invoice discounting over SWIFT, also integrated with SAP
- 'Intelligent Receivables' for automated reconciliation of customer initiated payment transactions in the Distributors channel
- An e-collections platform using the new 'Automated Clearing House' (ACH Debit) module of National Payments Corporation of India (NPCI)

The Results

This was a complete transformation project that touched all parties of the value chain, resulting in HUL building cash management processes that can be scaled up to support the agenda of rapid growth and transaction proliferation. The entire change was delivered within a 'business as usual' environment without any disruption.

With the integrated cash management structure, HUL has achieved a significant simplification of their banking operations across the organization. This includes:

- Reduction of bank accounts across the group's various legal entities
- Use of SWIFT and a treasury management system to simplify back office operations. Paper-based transaction initiation was eliminated through a combination of MT101 and MT320
- Automated bank reconciliations using the MT940 module linked to SAP

Other key benefits include:

- Electronic payments and collections
- Elimination of manual effort
- Substantial reduction in bank charges
- Improved end-to-end cash visibility to support daily liquidity planning
- Tighter liquidity management leading to reduced idle funds
- Sustained negative trade working capital with improvement in cash conversion cycle

This was a complete transformation project that touched all parties of the value chain, resulting in HUL building cash management processes that can be scaled up to support the agenda of rapid growth and transaction proliferation. The entire change was delivered within a 'business as usual' environment without any disruption.

KEYSIGHT TECHNOLOGIES INC.

Establishing a Globally Integrated Treasury and Banking Structure

In 2014, Keysight Technologies Inc. (Keysight) embarked on a year-long journey to establish a globally integrated treasury and banking structure. The end result was one of the most advanced, best-in-class treasury models in the industry, enabling Keysight to be operationally efficient and scalable for growth from day one.

The Challenge

On September 19, 2013, Agilent, the world's leading measurement company, announced plans to spin-off its electronic measurement business into a new company called Keysight Technologies Inc. Keysight has more than 9,500 employees serving customers in 100-plus countries.

The execution plan and key milestones of the spin-off was aggressive, including the formation of Keysight as a separate operating entity by August 2014; trading on the New York Stock Exchange by November 3, 2014; and a complete clean production go-live final cut-over from Agilent by December 23, 2014.

To support Keysight's spin-off strategy and objectives, the treasury teams of Agilent and Keysight partnered with Citi, their global cash management and trade bank, to implement an integrated working capital management solution covering cash management, liquidity and investment, trade services and finance, and commercial cards, across 30 markets globally, including nine countries in Asia Pacific.

The Solution

Keysight's global treasury and banking architecture was tailored to support the specific needs, challenges and ecosystem across several key functional stakeholders – including (but not limited to) the commercial business, treasury, global sourcing, shared services center, financial services and accounting, information technology, tax and legal.

In January 2014, a Singapore-led project team from Keysight and Citi was established as the central command post for project oversight, control and execution. Cross-regional and cross-functional teams across Asia Pacific, North America, Europe and Latin America regions, collaborated to ensure a seamless and successful global implementation, towards a common goal of achieving key milestones ending with a final go-live date of December 23, 2014.

The comprehensive solution set is comprised of the following key components:

- **Global credit facility** – Citi established a "Follow-the-Sun" program to optimize aggregated global clearing limits by transferring excess capacity back-and-forth, across regions and time zones to support Keysight's day-to-day cash management activities around the globe. Required facilities supporting the global card program were also put in place.
- **New account opening, legal entities name change, novation of operating accounts, banker guarantees and relevant documentation execution** – Globally, this involved over 230 accounts across 30 markets. In Asia, this included 100 accounts across nine markets. Global co-ordination was centrally managed from Keysight's global treasury center in Singapore.
- **Integrated cash management solutions** – A combination of domestic, and cross-regional, automated end-of-day, daily target balancing cash pooling structures were established with Keysight's global treasury center in Singapore as the pool header.
  - This approach involved 15 local currency pools globally with an overlaying group credit interest optimization solution in Asia Pacific.
  - USD and EUR are further concentrated to a single global cash pool in London on a daily basis, with good value dating through a "Follow-the-Sun" sweep - all delivered through Citi's robust single global concentration engine.
  - In Asia Pacific, a group credit interest optimization program was also implemented to further enhance the group total yield of returns for the region.
  - SWIFT FIN and FileAct were implemented to support Sungard's Integrity for making and recording treasury and intercompany funds settlement.
  - The integrated solution enables Keysight's treasury team to gain full visibility of cash flows, as well as consolidate and manage group daily cash positions across 37 legal entities and 27 countries globally, in a fully automated and efficient manner.
- **Integrated cash management solution** – Citi's extensive global network enabled the delivery of a full cash management service model to Keysight and its subsidiaries. A single, robust global host-to-host file based connectivity via Citiconnect for Files was fully integrated with Keysight's Oracle ERP to support straight-through payments and reporting reconciliation. Enabling a high level of process standardization and consistency to Keysight's India and Malaysia shared services centers. With market standard ISO XML version 3 file formats being successfully implemented for Western Europe to support Single Euro Payment Area compliance, and some elected countries in Asia, Brazil and Mexico, plans are under consideration towards achieving full standardization of file formats to the remaining regions.

To support Keysight's spin-off strategy and objectives, the treasury teams of Agilent and Keysight partnered with Citi, their global cash management and trade bank, to implement an integrated working capital management solution covering cash management, liquidity and investment, trade services and finance, and commercial cards.

Within the short timeframe of one year, Keysight established a world-class treasury model that delivers a high level of liquidity centralization, standardization and automation of process and reconciliation, information visibility and flows globally.

- **Integrated trade services and finance solution** – A customized trade document outsourcing solution (including letter of credit (LC), confirmation and discounting options, available on demand) was implemented, leveraging Citi's state-of-the-art online technology, experienced outsourcing team and vast corresponding banks global network. This solution supports the LC exports activities that are routed through Keysight's Singapore-based sales invoicing entity. Keysight is able to enjoy an end-to-end, operationally and cost efficient experience such as discrepancy-free first-party documents preparation, committed turnaround time, and dedicated trade services professionals and advisors to provide day to day operational support and advice to Keysight's credit control team.
- **Integrated commercial travel and expense card solution** – A globally consistent, locally compliant commercial cards program enabled Keysight to gain visibility and control of employee travel expenditures through an automated approval and reimbursement process. It further enabled Keysight's procurement team to analyze the volume and value of transactions to facilitate vendor negotiations. Through the execution of the global card program over 3,000 cards were issued across 27 countries and 37 entities. As part of the program, dedicated card services and account managers are assigned to provide on-going, all-round support and assistance to address enquiries from Keysight's Commercial program administrators and card holders.

The Results

Despite significant resource constraints and competing priorities, the implementation has been a great success, enabling Keysight to meet all their critical milestones, and objectives tasked upon the project team from both Citi and Keysight. The project was designed with a two-phase approach, aligned with the critical milestone of August 2014, and December 23, 2014 respectively.

For the first phase, the focus was to enable Keysight to gain banking and operational independence. For the second phase, the focus was on a massive technology and integration transformation involving Oracle ERP implementation and third-party vendor roll-out of global host-to-host connectivity.

Both deadlines were met and Keysight enjoyed a smooth transition in servicing its separated set of global customers and vendors, as well as employee obligations, seamlessly.

Within the short timeframe of one year, Keysight established a world-class treasury model that delivers a high level of liquidity centralization, standardization and automation of process and reconciliation, information visibility and flows globally. The fact that treasury was operationally efficient from day one is a significant achievement, taking into account complexities across Keysight's four distinctive regions (Asia Pacific, North America, Europe and Latin America), both in terms of legal entities structure requirements and the diverse jurisdiction and regulatory landscapes.

↑D79–D90
←D77

SHANGHAI ELECTRIC GROUP

Enhanced Treasury Management to Support Global Growth

By implementing a cross-border, foreign currency two-way cash pool with China, Shanghai Electric Group has achieved its cash management objectives as well as enhanced treasury management through managing the cash management needs of the domestic and international group companies more effectively, as well as managing financial risk across the group. In addition, treasury has a scalable framework in place to deliver additional value in the future, achieve its financial and operational objectives as they evolve and support strategic growth both in China and overseas.

The Challenge

As one of the largest equipment manufacturing conglomerates in China, Shanghai Electric Group Co., Ltd (SEG) has a leading position in its field, and is keen to achieve best-in-class status across all aspects of its business.

In 2014, SEG's treasury defined a series of objectives that would optimize its financial and operational efficiency, and position the group for future growth.

The first key objective was to leverage offshore financing more effectively to meet funding requirements within China, therefore reducing overall funding costs, streamlining cash management at a group level and increase funding diversification.

The second was to centralize cash and liquidity management at a group level, both domestically and cross-border, standardize and enhance efficiency and control in cash management, and improve access to group cash flow.

The Solution

Partnering with Citi and leveraging the recent cross-border deregulation in China, SEG implemented an automated, two-way cross-border foreign currency cash pooling structure.

By gaining the ability to leverage cash from across the group globally, SEG has been able to centralize cash management processes, both domestically and internationally, and has achieved greater control over cash flow. Furthermore, the solution aims to improve investment returns by maximizing the amount of cash available for investment, and reduce funding costs. End-of-day sweeping (for same day value) takes place automatically, therefore improving treasury efficiency and control.

The Result

By implementing the cash pooling solution, SEG achieved a range of advantages, both qualitative and quantitative. These include:

- As end-of-day cash sweeps take place automatically (with same day value), manual processing is reduced, eliminating the potential for fraud or error. Citi enables cash sweeps globally to have same day value thus treasury can maximize the return on funds held in the special account, increasing the yield on cash and enabling better management of counterparty risk. Similarly, by netting off credit and debit balances across the group, treasury has been able to lower its total cost of funding.
- Subsidiaries with negative balances benefit from lower financing rates by borrowing through the cash pool, while cash-rich subsidiaries gain a better return on their cash as cash investment can be performed at a group level, therefore increasing the amount of cash available for investment.
- In addition to the external financial benefits of the solution (i.e. lower financing rates, higher cash returns and lower external transaction costs), there have been important internal benefits, both tangible and intangible. By reducing manual processing, treasury resources can be allocated to more value-added tasks, as well as improving process control and auditability. Treasury has achieved better control over group cash flows, enabling a more efficient working capital strategy and facilitating further centralization. Furthermore, there have been FX risk management and quota advantages, further enhancing treasury's ability to manage group cash strategically.

While SEG had already achieved an impressive track record in FX risk management, its treasury was seeking to increase the mobility of its global cash, reduce financing costs, increase returns and optimize cash management at a group level.

By implementing a cross-border, foreign currency two-way cash pool enabled by deregulation in China, SEG achieved its cash management objectives, allowing its treasury to support the cash management needs of domestic and international group companies more effectively, as well as managing financial risk across the group. In addition, its treasury now has a scalable framework in place to deliver additional value in the future, achieve its financial and operational objectives as they evolve and support strategic growth both in China and overseas.

Partnering with Citi and leveraging the recent cross-border deregulation in China, SEG implemented an automated, two-way cross-border foreign currency cash pooling structure. By gaining the ability to leverage cash from across the group globally, SEG has been able to centralize cash management processes, both domestically and internationally, and has achieved greater control over cash flow.

TYCO INTERNATIONAL

Setting Up the Necessary Pipes to Bolster China Business Growth

With more than USD10 billion in annual revenues and 11 percent share of an USD100 billion fragmented market, Tyco is the world's largest pure-play fire protection and security company.

The Challenge

Tyco's growth strategy stems from its ability to drive recurring service revenue from a world-class customer base and leverage an expanding presence in high growth markets. With 65,000 employees in nearly 50 countries, Tyco has advanced safety and security for more than three million companies worldwide.

China is an important strategic growth market for Tyco, yet it is also a challenging market to operate in from a cross-border liquidity management perspective. To support growing operations in 20-plus Chinese cities, Tyco had to seek short-term domestic funding on a regular basis, while its surplus cash in China could not be accessed outside of China. The borrowing requirements within China incurred additional costs as well as administrative resources.

With ongoing RMB liberalization and the establishment of the Shanghai Free Trade Zone in 2014, Tyco saw the opportunity to tap intercompany funding (in RMB) into China on a streamlined and efficient basis as well as incorporating surplus cash in China into its global pool of funds. This has significantly improved their working capital management and enhanced operational efficiency within China.

The Solution

Partnering with Citi, Tyco implemented an automated two-way cross-border RMB sweeping structure, as one of the first pioneers of companies using an automated means to bring funds into China.

The company is now able to perform cross-border RMB sweeps from and into China on a true end-of-day basis from its finance entities outside of China.

Tyco chose Hong Kong to manage their RMB flows, as Hong Kong has the deepest RMB liquidity, which best suited the company's needs to convert surplus USD into CNH to fund their working capital position on a regular basis.

The Result

With the cross-border RMB sweeping structure in place, Tyco has managed to:

- Reduce external funding costs in China, and thus improved its balance sheet efficiency since reduction of their working capital cost translates into a higher return on assets
- Allocate resources previously spent on administrating the intercompany loans to other priority projects
- Access surplus funds in China

By integrating RMB into its global treasury management structure, the company has now established the basis for adding further treasury services to its Chinese entities. Integrating them into its global treasury management structures will support Tyco's long-term strategy in China, which is a growth market for its domestic sales and operations.

Tyco chose Hong Kong to manage their RMB flows, as Hong Kong has the deepest RMB liquidity, which best suited the company's needs to convert surplus USD into CNH to fund their working capital position on a regular basis.

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