Intercompany Liquidity Management Compliance: 10 Things

Basel III, proposed changes to US tax code section 385, BEPS and other regulatory rumblings pose challenges to common treasury management techniques such as cash pooling. Here are ten things that prudent global treasurers should undertake in the near term.

1. Review the capitalization structure of foreign entities to ensure that they do not fall under thin capitalization rules for that country.
2. Evaluate all intercompany loans to determine if any should be converted to equity capital. This could arise due to withholding tax impact on intercompany loans in certain countries such as Brazil.
3. Analyze intercompany lending agreements to make sure that tenor, payment schedule and rates of interest are correctly specified. Ensure that the rates of interest would be considered "arm's length", reflecting market conditions.
4. Maintain a record of all intercompany transactions in a central location such as a treasury database or spreadsheet. This will make it easier to respond to proposed and actual regulatory actions.
5. Where physical pooling arrangements are used, make sure that the intercompany loan documentation specifies that the pool header is acting as an agent not a principal in the arrangement. In any pooling arrangement, an underlying tax exposure may exist in some jurisdictions if a pool participant has a net payable balance in the pool for an extended period of time.

6. Interest charged and paid in physical pools should be based on bank data tracking movements to and from the header account and subaccounts. This can be done through the liquidity modules many banks have as part of their banking platform using a Treasury Management System or through the IHB module of an ERP system.

7. Assess intercompany payment transactions to ensure that they are settled within 90 days. Settlements extending beyond 90 days should be converted to loans and depending on the length of time in settlement can be considered equity.

8. If there is a high volume of intercompany transactions in different currencies consider multilateral netting. Current technology allows for this to be managed internally or through a third party.

9. Explore the tradeoffs between bank financing and intercompany funding. Absent tax and regulatory impact internal cash is always more efficient—but few global treasuries operate without certain tax constraints.

10. If notional pools are used to manage intercompany liquidity, now is a good time to review this approach. Basel III is raising the cost of this technique and Section 385 proposals appear to challenge the transparency of the approach. If notional pooling is maintained, ensure that cross guarantees are in place and that the overall pool position is brought to zero at least annually in order to avoid the appearance of long term loans.

ABOUT TREASURY ALLIANCE GROUP LLC

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