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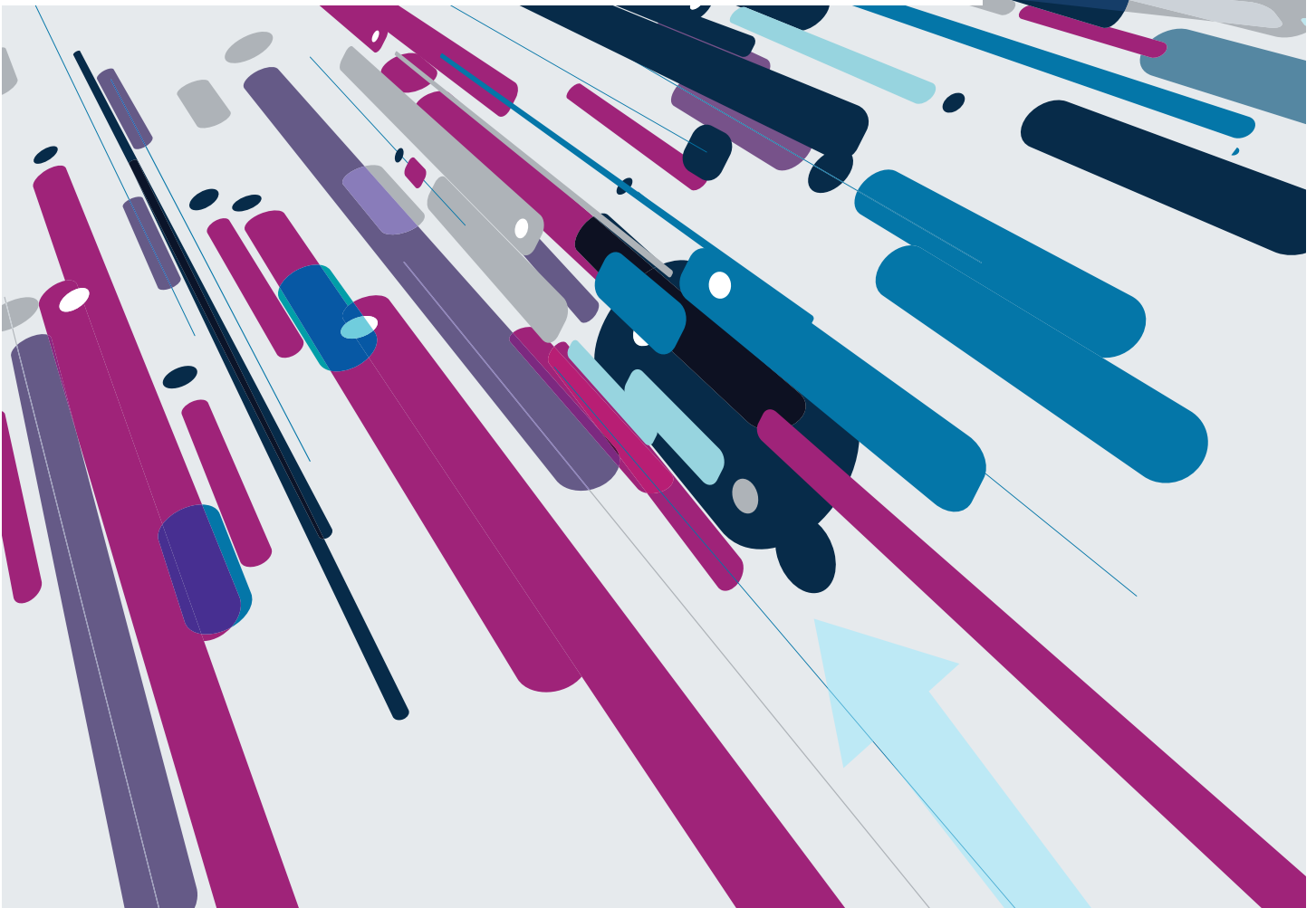
AFP EXECUTIVE GUIDE

# Concentrating Cash Across Borders

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# FOREWORD

The ceaseless flow of headlines shouts of supply chain disruptions, interest rate hikes, inflationary pressures, and even a looming recession. In the current climate, treasurers have found themselves waking up to what seems like a new and challenging situation every other day.

However, it is in such times that it is especially important to double down on the foundation of corporate treasury: cash management. It is important to take a step back and reassess objectives, identify and examine the root cause of problems, refresh the basics, and explore ideas and possibilities.

This guide, developed in partnership with the Association of Financial Professionals, will provide you with a practical and global perspective of how companies like yours are managing cash pooling across borders in this new norm.

As visibility, control, and optimisation remain unwavering needs in managing liquidity, the guide starts with a discussion on pooling objectives and the challenges faced by treasurers, before delving into the needs of establishing governance, leveraging technology, developing implementation plans, and measuring efficiencies.

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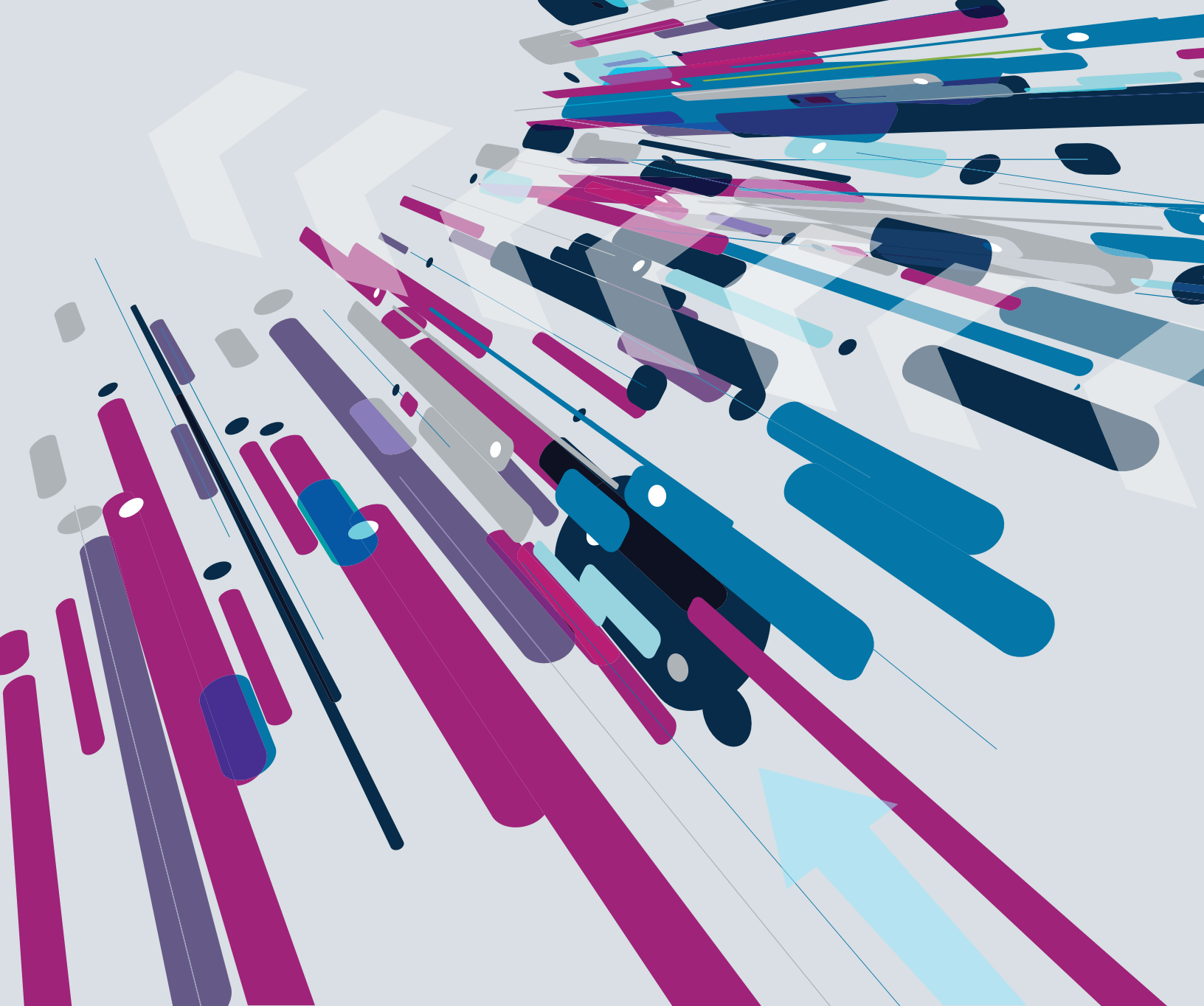
**Ankur Kanwar**

Head of Cash Products, ASEAN, and  
Global Head of Structured Solutions  
Development, Standard Chartered

**Sandrine Jourdainne**

Global Head of Deposits and Liquidity  
Management, Standard Chartered





# INTRODUCTION

With interest rates higher than they have been for fifteen years, the value of cash has risen too. A treasurer who can minimize external borrowing costs by utilizing internal cash efficiently will add real value to their organization. Cash concentration is an effective way to mobilize internal cash, with many companies doing so on an in-country basis. Today, a combination of technology and regulatory change means it is increasingly possible to concentrate cash on a cross-border basis too.

This guide outlines why treasurers are working to concentrate cash across borders and highlights, with examples from different regions, the significant barriers of doing so. It illustrates the importance of working with internal partners to achieve buy-in for a project to ensure it is as effective as possible. It discusses how treasurers can use external partners, banks and technology providers to facilitate cross-border cash concentration and concludes by looking at some trends for treasurers to watch.



# WHAT IS CASH CONCENTRATION?

Cash concentration is the practice of moving cash from bank accounts across an organization into one (or more) central account, generally known as a header account. The practice is simplest for a company operating in one country via a single legal entity. The task becomes more complex once cash managers want to concentrate cash from bank accounts held in the name of separate legal entities (i.e., bank accounts held by group subsidiaries, even if the ultimate beneficial owner of all the accounts is the same). Concentrating cash held in bank accounts in multiple jurisdictions in different regions can be very difficult, not least because of practical issues with managing activity across time zones. In addition, significant time may be required to prepare the cross guarantees and/or intercompany loan policies that underpin any cash concentration structure.

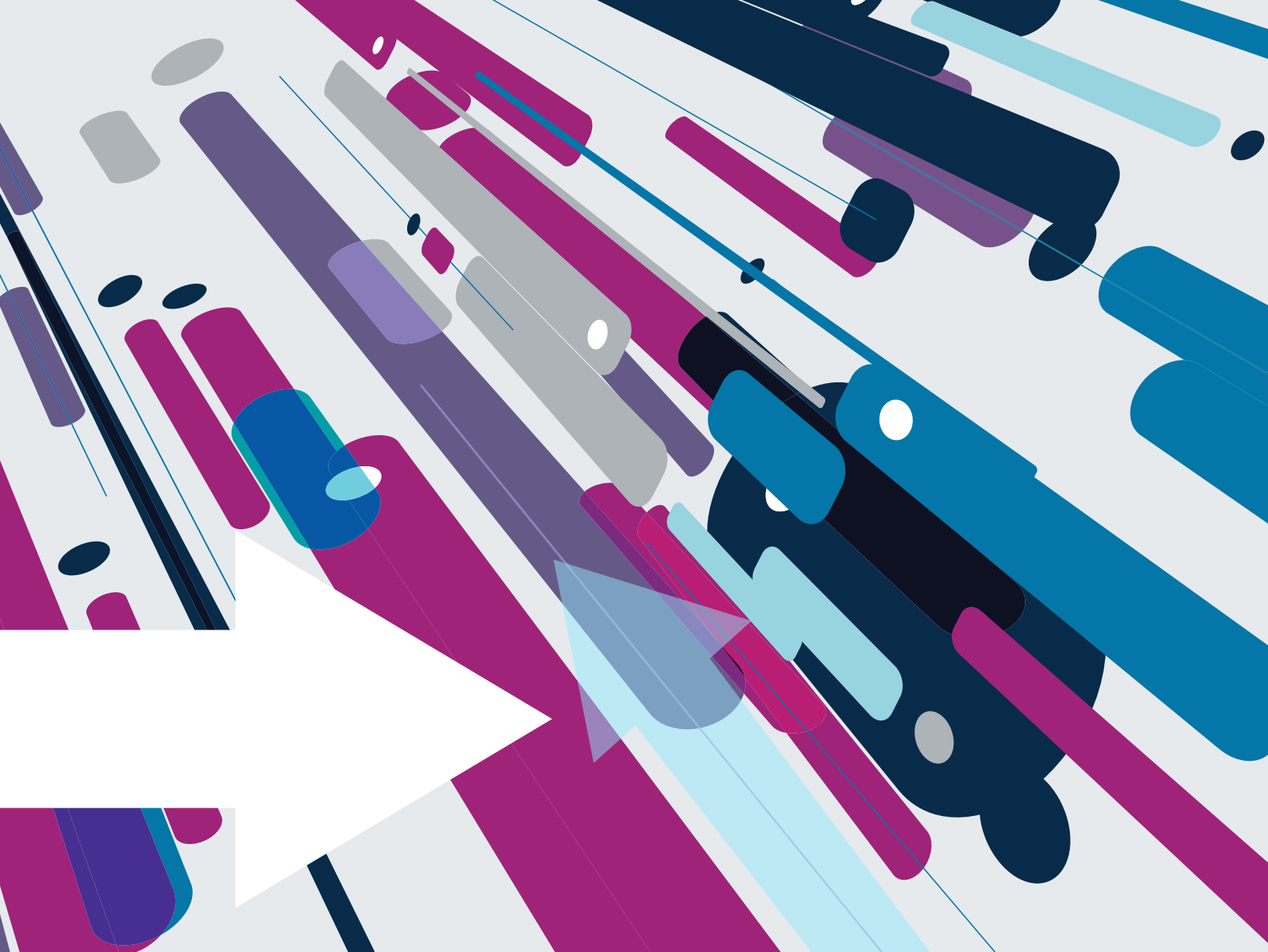
Three core techniques are used to concentrate cash:

First, cash can be **physically pooled**, i.e., transferred from one bank account to another. The transfer can be automated via a balance sweep to the header account, or an account can be set to be zero-balanced. Where functionality does not support automation, balances can be manually transferred between the header and participating accounts. Any physical transfer of funds between accounts held in the name of separate legal entities (e.g., between a subsidiary and a treasury center/HQ account) creates an intercompany loan.

Second, cash can be **notionally pooled** (depending on local regulations — for example, it is available in the Netherlands, Singapore, the UAE and the UK), whereby a bank treats two (or more) accounts as if the balances had been physically

pooled, but without the need for the physical transfer to take place. In this scenario, the balances on each account remain the same. Notional pooling is usually only available for bank accounts held with the same bank, so companies may need to physically transfer funds from other banks into accounts at the pooling bank for them to be included in the notional pool. The physical transfers can take place on an in-country basis, while the notional pooling is usually effected on a cross-border basis. (It can be difficult to implement a cross-border notional pool.) Some banks offer a multicurrency notional pool, allowing the participants to concentrate liquidity in different currencies without the need for foreign exchange transactions.

Third, some companies concentrate cash via a **virtual account network**. In this structure, the corporate HQ or treasury center holds the header account with a bank, where all eligible corporate funds are held. Under this account, the treasurer creates a network of virtual accounts (effectively a network of general ledgers) that mirrors the structure of the group as an in-house bank. Intercompany transactions can be settled via book entries on in-house bank accounts, with arm's length interest applied/charged on positive/negative balances. The use of an in-house bank enhances the efficiency of a group's liquidity management structure, as all intercompany cash flows, including bank account interest, are retained within the group. Some virtual accounts can be directly addressable (i.e., they have their own bank account routing numbers), so collected payments can be recorded in the virtual account (for ease of reconciliation) and physically received in the header account.



# ESTABLISHING THE OBJECTIVES FOR CASH CONCENTRATION

Cash concentration is an established liquidity management practice, especially on an in-country basis. Automated sweeps and zero-balancing accounts are common tools; for U.S. domestic companies, they date from the period when banks were prohibited from paying interest on current accounts. Recent technological and regulatory changes mean it is increasingly practical for multinational companies to establish cross-border cash concentration structures on a global basis, although, in many jurisdictions, a number of significant barriers remain.

## The changing environment

Today, companies are reviewing their approach to liquidity management generally, and to cash concentration specifically, driven by a number of factors:

- **The rising interest rate environment.** Relatively higher interest rates increase the value of cash by making raising funds more expensive. This incentivizes treasurers to make better use of internal cash to minimize their reliance on external borrowing. Using concentrated surplus cash to pay down debt can save companies significant interest cost compared with a few years ago.

- **Volatile currency markets.** Using internal cash more efficiently, particularly to manage intercompany positions, can help to reduce exposure to foreign exchange risk and, therefore, balance sheet volatility.
- **Wider access to enabling technology.** The cost of acquiring and implementing treasury management systems (TMS) has fallen dramatically; cloud-based TMS are within budget for a much wider range of companies than ever. Managing an in-house bank with a network of virtual accounts requires a TMS (or similar system) that has the required record-keeping capabilities. For example, any cross-border intercompany payments have to comply with OECD transfer pricing guidelines, so the technology needs to be able to calculate and apply arm's length interest for participants in cash pools to be compensated appropriately. Today's technology solutions can also support intercompany netting structures, manage payment factories, and help manage foreign exchange hedging strategies and accounting.
- **Regulatory change.** A number of governments provide incentives to multinationals to establish regional treasury centers, which can be used to manage the header accounts for cash concentration structures. Alongside these incentives, there has been an increase in the development of cross-border payment schema (such as the SEPA in Europe and the cross-border retail payment initiative linking Indonesia, Malaysia, Singapore and Thailand), which will likely deepen over time.

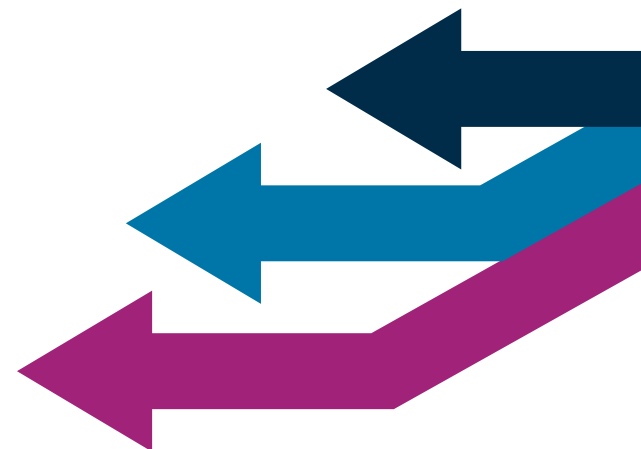
“In a high interest rate environment, surplus cash should be used to pay down debts to reduce negative carry or be deposited in high-yield current accounts to increase interest income.”

— Boon Long Oh, Treasury Professional, Singapore

## Value proposition

While the wider environment has made it easier to concentrate cash, cash concentration is only a part of a company's liquidity management strategy. Concentrating cash allows treasurers to meet wider objectives, such as:

- **Improved liquidity management.** By using surplus cash from cash-rich group entities to fund net borrowers, the (arm's length) interest rate spread is retained within the group as a whole rather than being used to reward an external lender.
- **Enhanced yield on surplus cash.** The potential benefit of an enhanced yield comes from the centralization of small pools of cash across an organization that are likely sitting in low-yield bank accounts. The centralized cash can be actively managed to obtain a higher return; simultaneously, the portfolio can be diversified to improve security and invested to support sustainability goals.
- **Reduced borrowing costs.** Using the corporate headquarters to raise finance is usually cheaper than enabling each entity to fund itself. The center typically has a higher credit rating than subsidiaries and is also usually able to tap a wider range of sources of finance.
- **Risk management.** Cross-border cash concentration can help to reduce foreign currency volatility, especially if cash is translated into the company's operating currency or if intercompany foreign currency payments are netted off.
- **Control.** Concentrating cash to the center may simply be part of a wider policy of treasury exerting more control over cash to improve operational efficiency. With improvements in technology providing visibility over cash and the ability to effect transactions remotely, central treasury can take control over much more of the financial supply chain than ever before.



## CASE STUDY: CLEAR OBJECTIVES ARE KEY

Setting a clear objective for a project is one vital driver for successful implementation and, ultimately, operational efficiency. For Parv Gill, Senior Treasury Director, Global Cash Management, at UPS, the group cash management objective is to maximize the level of cash that is moved back to the U.S. headquarters in Atlanta, Georgia.

A second driver of success is to have a forensic view of cash and how it flows through the business. With UPS, Gill categorizes three types of cash:

- Trapped cash, which is the cash that cannot be pooled in currency-controlled and regulated countries.
- Mobilized cash, which can be pooled and concentrated in UPS' in-house bank. This cash is available to be used across the wider business — for example, as intercompany loans, to support M&A activity, or to be “ready for deployment” for other business requirements.
- Freely available cash is all the cash that is at the U.S. headquarters.

UPS Treasury has been trying to create “Centers of Excellence” to standardize processes across all three regional treasury centers (Atlanta, London and Singapore). Gill is responsible for (among other things) global cash management and has implemented a two-stage process to repatriate cash to the U.S. headquarters.

The first step is to concentrate cash in-country to a header account, using whichever technique works best in each location, e.g., automated zero-balance accounts, cross-bank sweeps or manual sweeps with laser focus to eliminate manual processes.

Then, wherever possible, the in-country balances are brought to the in-house bank. Gill prefers to use physical pooling, although that leads to the creation of inter-company loans, which can be complex to manage from a tax and regulatory compliance standpoint. Where physical pooling isn't practical, notional pools with offshore bank accounts are used.

UPS operates three cash pools: two pools with U.S. dollar notional overlay structure (one in Asia, the other in Europe) and a European euro pool. The process starts with sweeping cash into the Asian pool — 75% of Asian poolable accounts are held with the bank operating the Asian pool, allowing for a true end-of-day sweep from those accounts. The structure enables automated sweeps from the pool into HKD and SGD demand deposit accounts held in Singapore. Residual balances are notionally drawn down in U.S. dollars and auto-swept to the European cash pool, allowing concentrated funds to be invested in various products.

Some currencies, such as the Philippine peso and the Thai baht, remain outside the pool. “In these circumstances, we invest funds in-country while we identify ways to repatriate and mobilize the cash,” Gill says. “So, for example, we have a dividend policy which requires treasury to maximize dividends for each business unit on an annual basis. Moving this cash through the structure maximizes cash we can return to the U.S. whilst managing FX risk and reducing FX volatility.”

Gill's principle: “If we can pool or mobilize cash, we will.” His approach is successful. “At present, we pool over 20 currencies across 37 countries, which covers 181 legal entities, with between 99% and 99.8% efficiency,” he says.



# THE NATURE OF THE PROBLEM: WHY IS IT SO HARD TO CONCENTRATE CASH GLOBALLY OR REGIONALLY?

Many companies are able to concentrate the major international currencies (i.e., U.S. dollar and Euro) both regionally and globally. For example, a large multinational with a presence in 100+ countries might have a series of cash pools: one in Singapore (for Asia-Pacific countries), another in Europe (for EMEA countries), and a third in the U.S. (for the Americas), with each one focused on pooling only U.S. dollar-denominated cash. Yet, despite the availability of cash

pooling solutions, it can be very difficult for companies to concentrate all their cash on a regional or a global basis, even if they choose a location for their header account that has few regulatory restrictions (such as the Netherlands or Singapore). There are multiple reasons for this — both regulatory and practical.

“Beyond supply chain shifts impacting cash pooling decisions, regulatory changes are another critical piece of the puzzle that can be challenging to keep up with. Treasurers should tap into the expertise of their banking partners to stay updated and ensure existing cash pool arrangements remain fit for purpose and optimized.”

— Ankur Kanwar, Head of Cash Products, ASEAN, and Global Head of Structured Solutions Development, Standard Chartered

## Regulatory issues

Local tax and financial system regulation can make it difficult or impossible for companies to include certain bank accounts in a cross-border cash concentration structure. Regulations vary between countries, with the most common sources of regulatory restriction on cross-border cash concentration being:

- **Currency restrictions.** Any currency restrictions will make it difficult to establish a cross-border cash concentration structure. For example, exchange controls may prohibit or restrict the transfer of currency across borders or the translation of local currency into a foreign currency (e.g., U.S. dollar) for pooling purposes. Collectively, currencies that are not freely convertible for foreign currency are sometimes referred to as “blocked” currencies, with examples being the Brazilian real and the Indian rupee. If a company needs to pay an invoice in a foreign currency, it may need to provide the invoice as documentary evidence of the liability before it is permitted to access foreign currency.
- **Bank capital requirements.** Without the right to offset a debit balance with a credit balance in the event that a client fails to repay an overdrawn account, banks may not offer notional pooling without charging for any regulatory capital it has to hold against the liabilities.
- **Transfer pricing.** OECD transfer pricing guidelines are designed to prevent companies from transferring profits from high-tax jurisdictions to low-tax jurisdictions. They require companies to apply arm’s length pricing on cross-border intercompany payments, such as the intercompany loans created by a physical cash sweep. Treasurers need to

document decisions on intercompany credit risk, apply arm’s length interest rates to internal transactions, and have an accurate record-keeping process so that the company can demonstrate compliance with any interested tax authorities, all of which require dedicated processes and systems.

- **Withholding tax.** Many countries apply withholding tax on cross-border payments, most notably on interest expense, dividends and royalties (where a subsidiary is making royalty payment to the parent for intellectual property purposes). Withholding tax can make it uneconomic to concentrate cash via regular sweeps, although companies will take their own positions on whether it is economical to repatriate cash annually via their dividend policy.

## Operational considerations

Some practical considerations arise from these regulatory concerns.

- **The management of non-convertible and less frequently traded currencies.** By definition, there is no market for non-convertible currencies, so they cannot be included in a cross-currency pool. In theory, other “exotic” currencies (currencies that are not regularly traded, e.g., the Ethiopian birr or the Qatari rial) can be traded and repatriated. However, the lack of a deep market can make any foreign exchange transaction difficult to manage and, in some cases, non-convertible in practice and, therefore, too difficult to include in a cash pool. In addition, the value (in the company’s operating currency) of both types of currency can be very volatile, so holding cash in such currencies can represent a significant financial risk.

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<sup>1</sup>The IMF publishes an Annual Report on Exchange Arrangements and Exchange Restrictions that includes details on currency restrictions. [www.imf.org/en//Publications/Annual-Report-on-Exchange-Arrangements-and-Exchange-Restrictions](http://www.imf.org/en//Publications/Annual-Report-on-Exchange-Arrangements-and-Exchange-Restrictions)

## CASH MANAGEMENT IS ONLY ONE COMPONENT OF TREASURY MANAGEMENT

Treasurers often have to manage competing objectives when designing their department structures, resulting in some solutions that are not optimally efficient. As Hisham Abouldahab, Corporate Treasurer, MAG, Egypt, explains, “Ideally, we would have a single cash management bank. However, we need to have a multibank solution to ensure we have access to sufficient liquidity to fund our trade shipments.”

Other factors often get in the way of the optimal structure too. “We have tried to set up a ZBA structure, but it hasn’t been possible,” says Abouldahab. “For example, in Uganda, we have to provide documents to support a cross-border transaction, making cross-border cash concentration impossible.”

Access to foreign currency can be a problem too. “In Ghana, there is a shortage of international currency, making it difficult to repatriate cash. In Egypt, we have to find sufficient hard currency to repay our shareholders. Our solution there was to open an offshore account in local currency to repay them,” says Abouldahab.

- **Internal credit risk assessment.** In order to set internal interest rates, treasurers will need to determine an internal credit rating for each participating entity so that an arm’s length interest rate can be applied. Companies will need a consistent methodology, similar to one used by rating agencies, to do so. Treasurers will then need clear advice from banks and auditors on how to set the rates based on these ratings, and from banks and/or technology providers on how to record and apply the set rates. Any company that is used to basing their internal interest rates off USD LIBOR will ideally have already altered their methodology and will have until September 2024 (when the synthetic rates will no longer be provided) to finally do so if they have not.<sup>2</sup>
- **The design of the cash concentration structure.** Generally, the greater the number of countries a company has a presence in, the more complex the cash concentration structure will be, not least because market regulation and general market practice can vary significantly between countries. For example, cut-off times can vary significantly between markets, as can the value of payments that can be settled in real time, making it difficult to develop a standard set of operating procedures. In addition, a structure covering multiple countries across the world can be difficult to manage simply because of the impact of different time zones and the existence of different national holidays.

“We collect deposits from business units globally via a cash pool which are on-lent to business units with working capital needs. The interest differential represents our profit margin which is used to pay off the treasury operating costs.”

— Boon Long Oh, Treasury Professional, Singapore

<sup>1</sup>The IMF International Financial Statistics (data.imf.org) includes a list of reference rates on a country-by-basis. Reference rates are also available from a number of other commercial providers.



# ESTABLISHING THE GOVERNANCE STRUCTURE

“A complex geopolitical environment and operational considerations make visibility and managing cross-border flows an even more strategic need for the business, which requires multiple account structures and multicurrency capabilities in place. Furthermore, having to deal with multiple providers and tech integrations makes it even more complex, and in this context, having a trusted bank supporting centralized integration makes a huge difference.”

— Sandrine Jourdainne, Global Head of Deposits and Liquidity Management, Standard Chartered

Given these general hurdles, each company faces its own particular challenges when seeking to establish a cross-border cash concentration structure. Doing so will require interaction from both internal stakeholders (e.g., tax, accounting, as well as the business units) and external partners (e.g., banks, auditors, technology providers). To be able to design an effective solution, treasury will need to be able to articulate the key parameters to the various other parties. These factors include:

- **Treasury structure.** The extent to which the treasury department is centralized (whether on a global or regional level) will influence the degree to which treasury can require group entities to participate in a cash concentration structure. Even where the treasurer has a mandate to insist group entities participate in a particular structure, managing internal relationships to maintain trust once cash is controlled at the center is vitally important for a successful project.

“Understanding the role of the pool leader is crucial. In most cases, it is a genuine leader (i.e., all cash is concentrated there). However, sometimes, due to certain local regulations and the overall pool structure, it acts as an agent wherein it is compensated by a management fee calculated at a certain percentage of the average assets (deposits) under management. This eventually makes the whole interest allocation process all the more complex.”

— Naved Akhtar, Senior Treasury Manager, United Arab Emirates

- **Existing procedures.** Although transition can be difficult, companies that have successfully migrated to a more centralized model (e.g., via the use of shared service centers or the implementation of a payment factory and/or in-house bank) will be in a stronger position to extend the concentration of cash on a cross-border basis. While some entities may be required to remain out of the centralized structure initially, they can be more easily incorporated should regulations or other factors change to permit participation.
- **Missing elements.** Irrespective of the level of centralization, treasurers will need to identify any gaps between the current and the required structures. Treasury will need to work internally with tax and legal to find solutions to bridge those gaps — for example, if a new legal entity is required to own the new header account.
- **Existing bank relationships.** It will be easier to manage a regional or global cash concentration structure if all accounts are held with the same bank. However, large multinationals often prefer to appoint a number of cash management banks, whether because they have adopted a “best in class” service method, need to access credit lines, or to want to mitigate bank counterparty risk. Whatever the rationale, once treasurers have to include multiple banks in their cash management structure, it becomes more complex to manage efficiently.

## CHOOSING THE LOCATION FOR THE HEADER ACCOUNT

To maximize the benefits of cross-border cash concentration, treasurers need to determine the appropriate number of header accounts (i.e., the number of cash pools) and then decide the most appropriate location for each one. Vinit Mishra, Head of Treasury, Finance and Insurance, at Absolute, has decided to establish a single cash pool initially, as he feels having multiple cash pools can reduce the potential liquidity benefits from pooling, e.g., by not fully minimizing bank transaction costs, cost of finance and foreign exchange risk. Although Absolute is headquartered in India and generates the majority of its revenues there, the pool will be located in either Singapore or the UAE. This is, in part, due to India’s restrictive local regulations on foreign currency transactions, cash pooling and tax, and also because the company is expanding rapidly internationally.

“Once you get the business into the mindset that cash is a corporate asset, it is easier to implement change.”

— Parv Gill, Senior Treasury Director, Global Cash Management, UPS

## Planning the structure

Careful planning is required to ensure the new structure is as efficient as possible. The planning process is likely to consist of these key stages:

### STAGE 1. SETTING THE BIG PICTURE

**Whether it's a brand-new plan or a redesign, the cash concentration structure needs to fit the company's treasury strategy and operational model.**

- How is liquidity managed now? Can in-country liquidity be managed more efficiently? Will cash be concentrated on a global or regional basis? How will in-country cash be moved to the center (e.g., via an overlay structure)? Does the company have (or plan to have) an in-house bank?

### STAGE 2. SHARE THE VISION

**Build buy-in with internal stakeholders** — these should include leaders (i.e., CFO, head of tax, head of legal, etc.) as well as the business units. Show how concentrating cash will improve the business.

**Meet with external partners to talk through the plan.** Try to understand the implications of regulation for the proposed structure. Talk to banks about their functionality and ability to support the project.

### STAGE 3. DESIGN THE PLAN

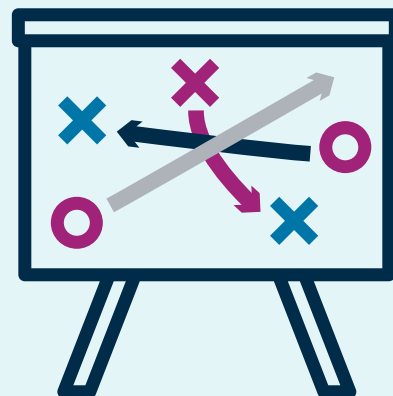
**What will the structure look like?**

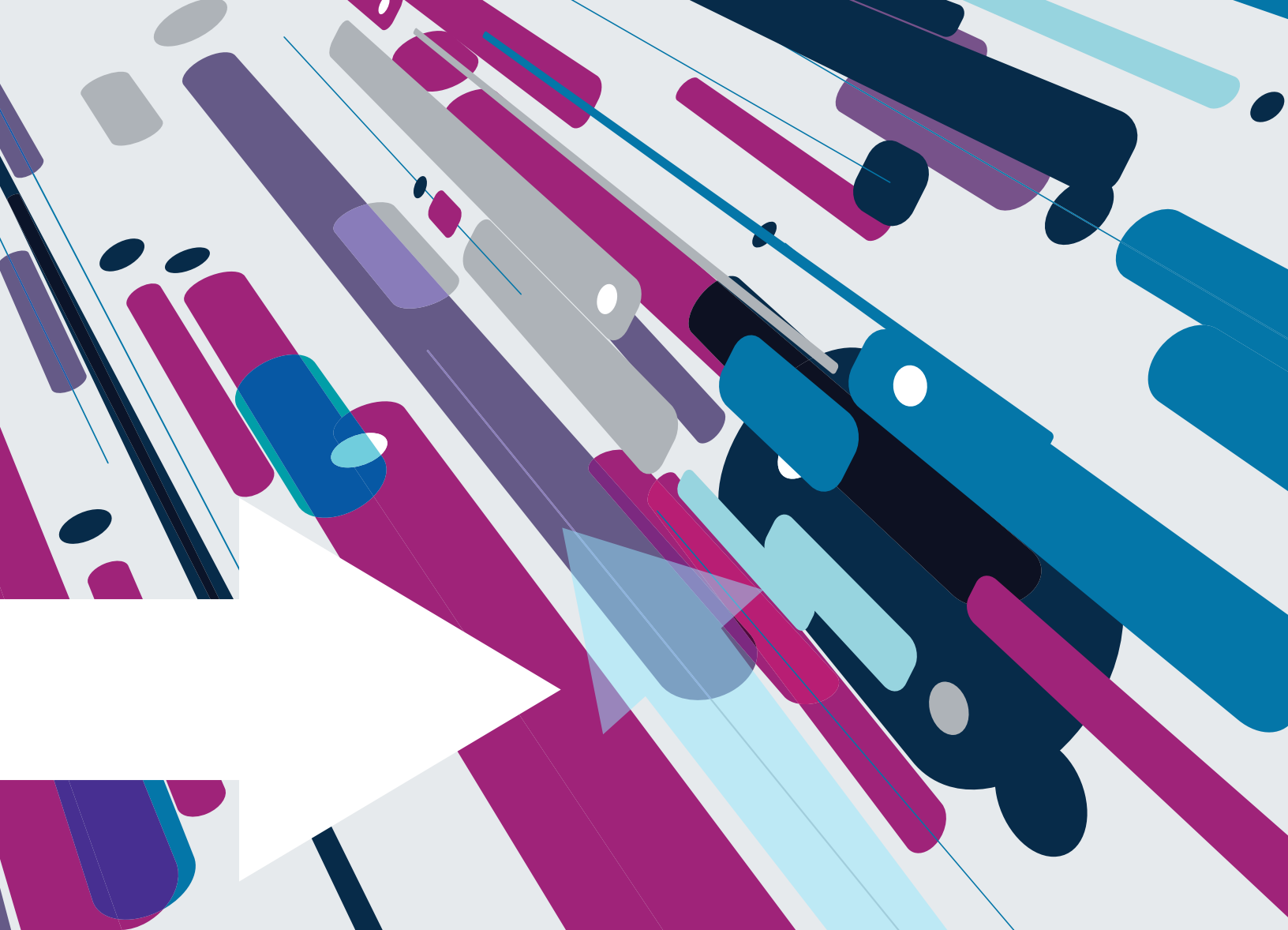
- Which jurisdictions and currencies will be included? How will those that are not included be managed? It is usually possible to concentrate that cash on an in-country basis.
- The account structure — where will the header account(s) be? More countries are offering financial incentives for companies to establish regional treasury or finance centers, making them potentially attractive for the location of the header account. How will sub-accounts link to the header? What are the legal and tax considerations?
- Cash concentration techniques — which ones will work best? How will intercompany loans be managed? When will cross-guarantees be needed? Is intercompany and/or third-party netting included in the project?
- What reporting is required, both centrally and in each country? How will the company demonstrate compliance with local regulations and accounting rules? What processes are in place to rate internal credit quality and apply appropriate reference rates to internal transactions, e.g., to intercompany loans and notional and virtual account balances?

### STAGE 4. IMPLEMENTATION

**How will the company move from its current structure to the new one?**

- Keep internal stakeholders engaged.
- Set a timetable for transition.
- Track and report progress to all key stakeholders.
- Celebrate success by quantifying if possible.





## EXECUTION OF THE PLAN: THE ROLE OF THE BANK

Banks have a central role in the execution of the cash concentration structure, irrespective of the specific design of the company. The core role — which is easily overlooked or taken for granted — is the provision of the company's bank accounts themselves. Even with companies that operate virtual account networks via their treasury management system, there is always at least one header account that is held with an external bank (i.e., a regulated financial institution) and acts as the gateway for making and receiving external payments, and for receiving funding and paying down external debt.

Certain parts of the cash concentration cycle have become commoditized over the years, notably the provision of cross-border payment services by specialist payment providers. The implementation of an effective and flexible cross-border cash concentration structure remains one where corporate treasurers rely on their partner banks to deliver dedicated solutions. As well as being implementation partners, treasurers also need their banks to act as trusted advisors. Treasurers will want banking partners that can advise on the most appropriate solution to support their requirements and the functionality to be able to support its implementation.

“Our clients are increasingly leaning on us to share knowledge and the latest beyond our solutions. They value the expertise we bring on related areas such as new treasury structures, regulatory insights and technology/platform partnerships.”

— Ankur Kanwar, Head of Cash Products, ASEAN, and Global Head of Structured Solutions Development, Standard Chartered

There are some key points to consider when choosing a bank to support cash concentration.

First, a treasurer will benefit from first trying to understand how regulations affect the scope for cash concentration in each relevant market, and then working to find a provider that can offer the full range of permitted capabilities, with the ability to update its solution as regulations change.

Second, look at the footprint of potential banking partners compared to your own organization. Also, check the functionality of potential banking partners in each relevant jurisdiction. Just because a bank provides a particular service in one jurisdiction, it does not mean it will provide the same service in others, even if it has a presence. Bank services often vary between countries due to the nature of their client base in each location.

Third, look in detail at the potential banking partners' liquidity management offering. Does the bank have the ability to meet your needs in every location? How will the bank provide support when the ideal solution isn't available? (Some techniques are prohibited in certain locations, or the bank may not have a particular capability in another.)

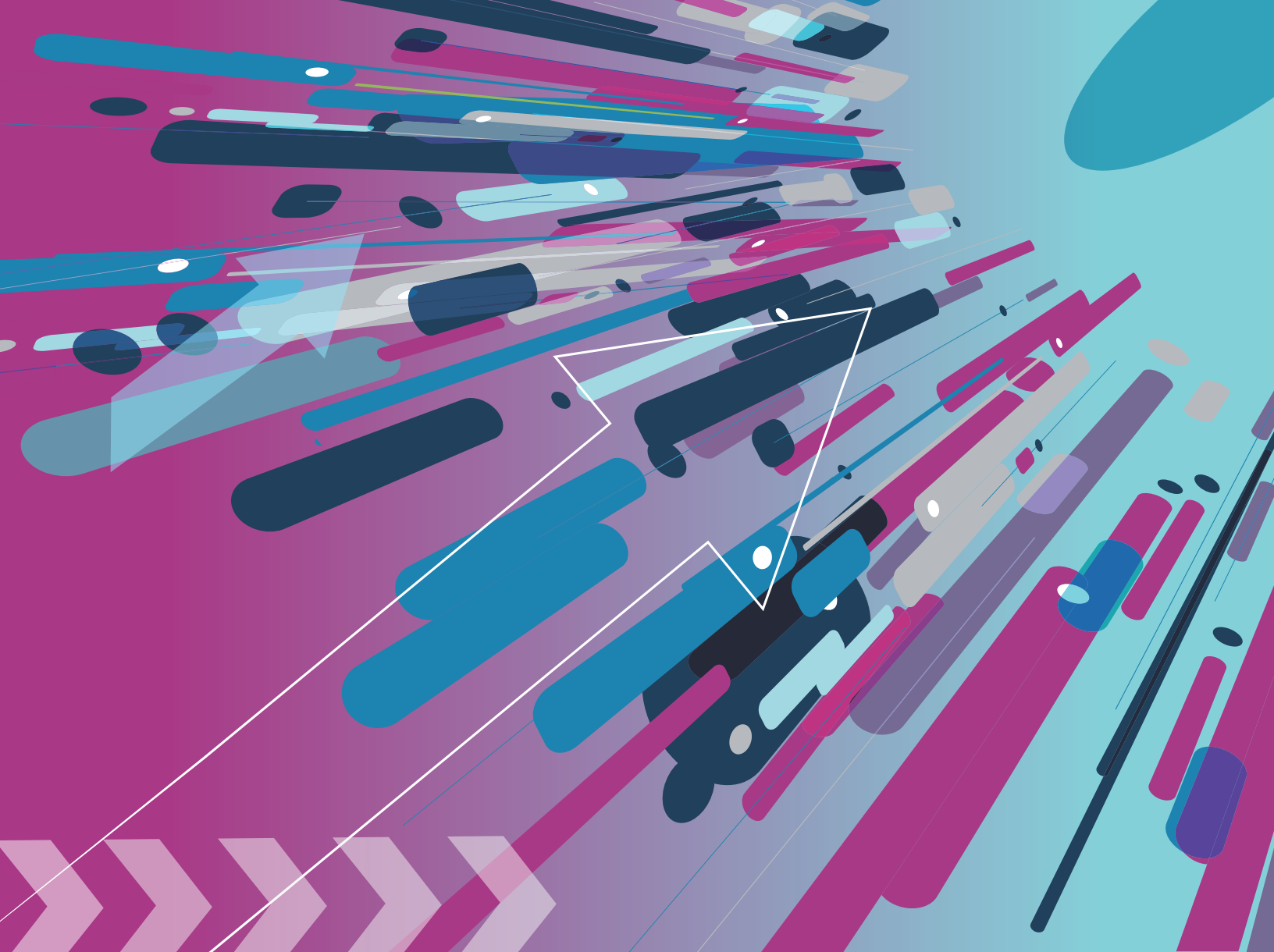
Fourth, consider how you will communicate with each potential banking partner. A seamless integration between the company and the bank can be a significant benefit, as long as the bank can support the delivery of treasury's overall goals.

Finally, keep in mind that banks need to generate income by creating new products. Bank innovation in response to regulatory change and client demand will help open new opportunities for treasury to improve operational efficiency. Meet with potential banking partners to understand how they work with clients and whether their approach will benefit you.

Banks play a pivotal role in enforcing central bank regulations that cover cross-border payments. As Isha Goel, a Senior Treasury Professional based in India, explains, “In India, the central bank issues the regulations but leaves some of the details to [commercial] banks to administer. Our relationship bank mandates for documentary proof that a proposed or requested payment is legitimate. They have a compliance team that is responsible for checking that the evidence we provide matches with the requested payment to be processed. If they aren't satisfied, they won't process the payment or they will ask for further proof to support the payment.”

Even though there are techniques available to minimize the number of cross-border payments, these can have drawbacks if not backed by sufficient support or evidence. For example, while it is possible to net receivables and payables, Goel says that “this can make responding to regulatory scrutiny, if any, difficult, especially at a later stage. So [in India], many companies prefer to settle each invoice separately to ease reconciliation.”

If surplus cash cannot be pooled centrally, it needs to be managed locally and there may be a foreign currency position to be managed. For example, if receivables are denominated in local currency and payables in foreign currency, companies need to consider how best to hedge the positions.




# THE IMPORTANCE OF PROPER REPORTING AND RECORDKEEPING

In addition to the banking partners, technology is the other key component in a successful cash concentration structure. Technology plays a key role in managing any cash concentration structure for two reasons. First, to be as efficient as possible, treasurers want access to accurate and timely information. Second, to demonstrate compliance with tax and regulation, companies need to apply and record their transactions on a consistent basis.

### Real-time reporting

The evolution of technology has transformed liquidity

management practices across all types of organizations. As an example, payment settlement times have accelerated, such that same-day and instant payments have become much more widely used, as part of a shift to various types of electronic payment. Alongside this acceleration, treasurers are increasingly able to access transaction and balance information in real-time, providing visibility of cash. With real-time information, treasurers can have greater confidence that, when concentrating cash, the data they rely on is as accurate as possible. The result is that the balances that remain “idle” are minimized, ensuring internal cash is utilized effectively.



To create a real-time reporting environment, treasurers have to prioritize three things:

- **Choice of technology platform.** Whether treasury uses a TMS, an ERP system or a standalone solution, the platform must be robust enough to be able to process data in real-time.
- **Data feeds.** The reporting is only as good as the timeliness and quality of the received data. The use of APIs can ease the process of collating transaction data from banks, especially for organizations that have multiple banking partners.
- **Bank functionality.** Treasurers need to understand how frequently their banks can supply transaction data. An increasing number of banks can provide data in real-time (or within a few minutes); however, others may only provide certain data on an end-of-day basis. While it may be preferable to select banking partners that can provide real-time data, it may not be practical in certain markets where other factors are more important. The key is to know which data is not available in real-time and adjust the decision-making process accordingly (e.g., by relying more on forecasts when concentrating cash and holding higher precautionary balances to protect against the risk of inaccuracy).

For Naved Akhtar, a Senior Treasury Manager based in the United Arab Emirates, seamless data integration between entities in a cash pool and the treasury platform is crucial. The availability of daily pool balances and interest accrual reports from the banks is very important. “If you are not getting the right reports at the right time, the overall functioning of the pool may get impacted,” he explains. “Check your banks are capable of providing the reports you need.”

## Record-keeping

While active cash and liquidity management requires real-time reporting, demonstrating compliance with transfer pricing rules when concentrating cash across borders is critical to avoid scrutiny and sanctions from multiple tax authorities.<sup>3</sup> To do so requires access to a platform that can apply arm’s length interest accurately in a way that is consistent with the company’s own internal credit ratings and create an audit trail that will satisfy any external scrutiny. This functionality is available from banks or via the company’s treasury management system.

Treasury will also need an efficient reconciliation process, especially if treasury operates as an in-house bank. This will help to ensure any received payments are allocated to the appropriate account. Where regulators require documentary evidence before permitting cross-border transactions, an accurate matching process between invoices and payments can ease what can be a complex compliance process.

<sup>3</sup>The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022 are available at [www.oecd.org](http://www.oecd.org).



# MEASURING THE EFFICIENCY OF THE STRUCTURE

With the treasury environment constantly evolving, whether through technology innovation, regulatory change or market volatility, treasurers remain under pressure to continually improve operational efficiency. With respect to cash concentration, two questions stand out. First, how can treasurers measure whether the cash concentration is efficient? And second, how can treasurers leverage their investment to gain further efficiencies, given their objectives for the structure?

## Efficiency measurement

Cash concentration is a tool used to achieve other objectives, so one way to measure efficiency is to determine whether those higher-order objectives have been met. Treasurers may set, or be set, some key performance indicators, including some of the following:

- **Level of concentrated cash.** What proportion of cash balances in participating accounts is collected to the center?
- **Optimal use of internal cash.** Has cash concentration allowed the company to minimize borrowing costs or enhance its yield on short-term surplus cash? What have been the effects on working capital?
- **Effective foreign currency risk management.** Have foreign currency exposures been netted internally to minimize the requirement for external FX transactions?
- **Cost optimization.** Has cash concentration allowed treasury to reduce banking costs (e.g., transaction

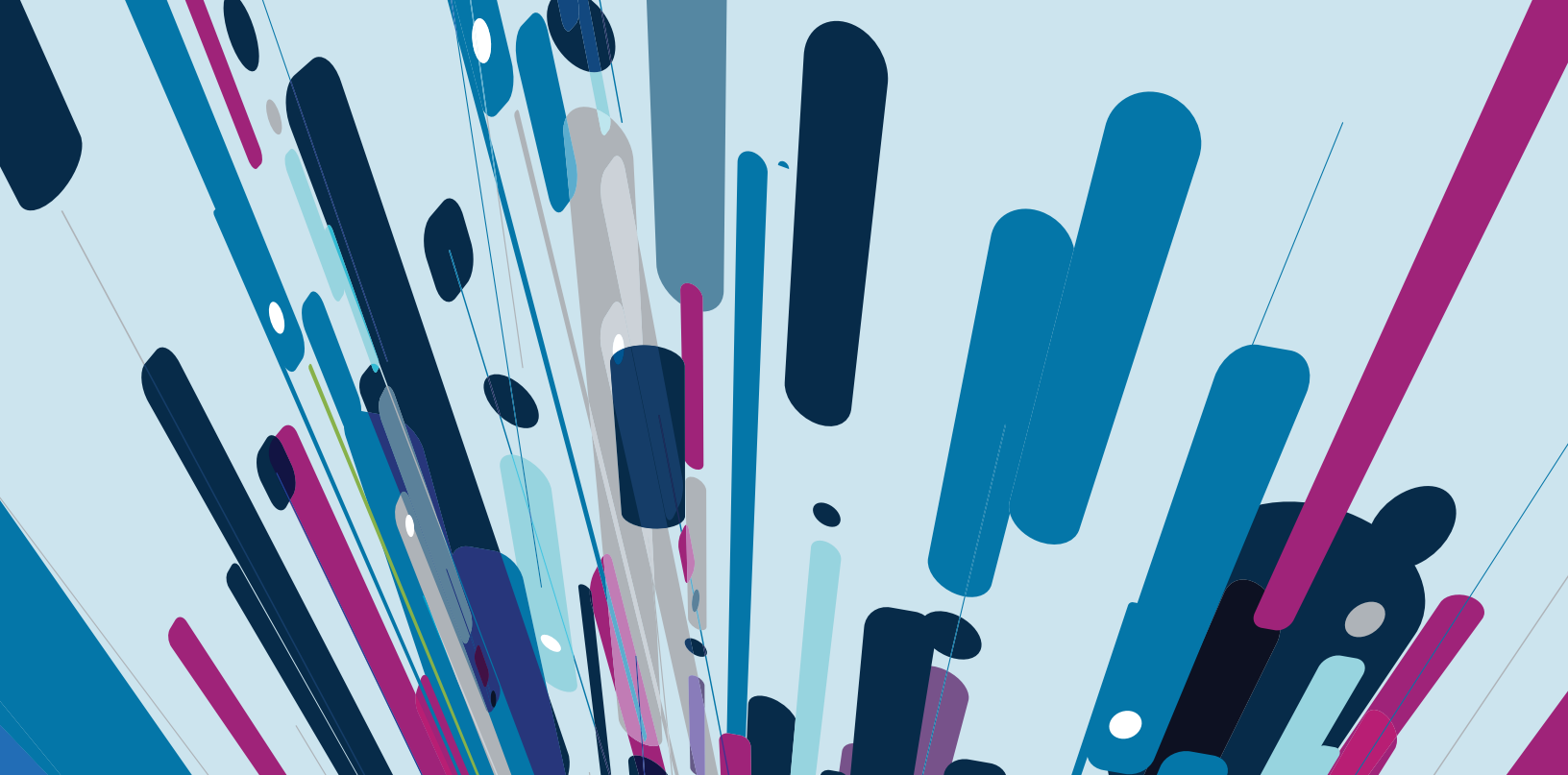
costs, FX transaction costs and account fees) and/or rationalize the banking group? What has been the impact on operational costs (e.g., treasury headcount, bank relationship management efficiency)?

## Extending the gains

Given an investment in a cash concentration structure, there will usually be opportunities to gain further efficiencies. The most common are:

- **An extension of intercompany netting** to include third parties on both the payables (i.e., vendor) and receivables (i.e., customer) sides.
- **Other centralization opportunities**, e.g., to manage payments (and/or collections) on behalf of group entities from an in-house bank or payment factory.
- **Integration opportunities.** As data flows between banks and their clients improve, treasurers have greater opportunities to link payments and funding via their cash concentration structure. Disbursement accounts within cash concentration structures can be set to zero-balance, meaning the cash pool can fund outgoing payments on a “just-in-time” basis. Greater accuracy in cash forecasting via solutions incorporating integrated data and AI can help ensure the pool can fund those disbursements.

The degree to which further efficiencies can be realized will depend in large part on the nature of the organization, its cash flows and the jurisdictions in which it operates.



## WHAT'S NEXT?

No cash management structure will remain efficient without the facility to adapt to new market conditions and meet its organization's changing needs. There are a number of areas where market change will provide opportunities for treasurers to achieve efficiency gains, irrespective of their internal structures today.

**First, the availability and uptake of centralized solutions continue to increase.** For instance, while in-house banks have been largely used in the European market, they are becoming much more common globally, with significant increases in, for example, Hong Kong, Singapore and the U.S. A number of countries are encouraging companies to establish regional treasury centers or in-house banks via the provision of financial incentives such as a reduced withholding tax liability.

**Second, technology continues to evolve, with deeper functionality available at lower cost.** The availability of APIs is enabling a more efficient transfer of data, notably between banks and their corporate clients. Treasurers have access to instant or near-real-time data reporting from their banks, and there are multiple innovations along the whole financial supply chain, such as the increased use of QR codes for B2B, as well as C2B, payments.

**Third, these technology developments are also driving change in business models.** Instant payment schema is available in many more countries. Although the uptake is largely within the consumer space to date, this is often due to initially relatively low payment value thresholds when a new scheme is launched. As thresholds increase, instant payments become a more realistic solution for business-to-business transactions too.

**Finally, regulations are constantly changing, easing the process of concentrating cash across borders.** The challenge for treasurers is to understand how regulations are changing and what implications any changes may have for their cash concentration structure. Most changes are trailed in advance, so banking partners should be a good source of advice. Regular contact with banking partners will also identify new solutions that may further enhance efficiency.

Keep in mind that a structure that is efficient today will not remain suitable forever. So, when one change is required (e.g., to migrate to ISO 20022 payment types), it can be an opportunity to update other elements at the same time (e.g., to implement a virtual account network).



## CONCLUSION

The current market environment, with heightened interest rates and increased foreign exchange volatility, means treasurers can add real value to their businesses by utilizing internal cash as efficiently as possible. Access to more powerful technology and the impact of regulatory change means it is increasingly possible and practical to concentrate cash on a cross-border basis. Treasurers who want to do so need to work with internal stakeholders and external partners to design a solution that is efficient today and flexible enough to remain efficient into the future.

## TAKEAWAYS

“If you have cash, do what you can to mobilize it. Doing so requires rethinking and re-engineering processes through continued positive disruption.”

— Parv Gill, Senior Treasury Director, Global Cash Management, UPS

“Treasurers want to focus on their needs, but they also need a reliable banking partner — one that is knowledgeable, prepared to invest in solutions and offers a smooth implementation. These are critical ingredients needed to bring about transformational impact to the treasury function and broader organization.”

— Sandrine Jourdainne, Global Head of Deposits and Liquidity Management, Standard Chartered

## AFP Executive Guide: Concentrating Cash Across Borders

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PROFESSIONALS

All inquiries should be addressed to:

**Association for Financial Professionals**

Phone: 301.907.2862

E-mail: [AFP@AFPonline.org](mailto:AFP@AFPonline.org)

Web: [www.AFPonline.org](http://www.AFPonline.org)



## About the Authors

### Guy Voizey, WWCP Ltd

Guy Voizey has been a financial writer and editor for over 20 years. He is a director of WWCP Ltd, a research and publishing company, which specializes in the provision of information and editorial on corporate treasury and cash management. Guy wrote (or co-wrote) four books co-published by WWCP. In addition, Guy has also written over 20 executive and other guides for AFP, covering a range of topics, including liquidity management, cybersecurity, capital structure, taxation, and accounting. Guy edited the AFP's Essentials of Treasury Management (6th edition).



### Tom Hunt, CTP, Director, Treasury Services and Payments

Tom Hunt, CTP, is the Director of Treasury Services at the Association for Financial Professionals. Hunt has more than 15 years of direct treasury experience working across different industries, including various roles at Medtronic, Fairview Health Systems and, most recently, at 3M Company. At 3M, he oversaw the global banking strategy, redesigned and implemented a new domestic cash management structure and led acquisition activities for the treasury department. He holds an MBA in finance from the Opus College of Business at the University of St. Thomas in St. Paul, MN.

[thunt@afponline.org](mailto:thunt@afponline.org)



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12345 Parklawn Dr, Ste 200 | PMB 1001 | Rockville, MD 20852

T: +1 301.907.2862