Achieving Intercompany Accounting Excellence

Moving beyond traditional manual processes. Preparing for global regulatory change.

BLACKLINE

Digital Finance Transformation

PLAYBOOK

Increasingly complex multinational value chains, partly the result of industry consolidation or globalization, and more scrutiny from auditors and regulators are causing more and more companies to run into serious and costly intercompany accounting problems.

—AICPA / JOURNAL OF ACCOUNTANCY

Accounting in an Intercompany World

Intercompany transactions now represent the lion's share of the global economy—some 80% of global trade. And they're under increasing scrutiny. Transfer pricing is under the microscope, with tax jurisdictions becoming more aggressive when identifying issues and imposing penalties and fines.

Enterprises are strengthening cash management strategies by creating multilateral netting and further settlement procedures to reduce bank fees and better manage FX. Within entities, intercompany trade is also placing pressure on local accounting teams, who are facing growing numbers of associated reconciliations, which drains efficiency and often leads to rolling intercompany balances.

Corporate Accounting and Shared Service Centers

FAST FACTS

SPOTLIGHT ON INTERCOMPANY ACCOUNTING

CHALLENGES →

INTERCOMPANY TRANSACTIONS GROWING
80% of global trade now takes place within the value chains of large global organizations.[3]

LATENT RESTATEMENT RISK
Subsidiary and intercompany issues rank 5 out of 23 in the top reasons behind restatements.[4]

DISPARATE SYSTEMS
Disparate systems were the top intercompany accounting challenge, cited by professionals.[5]

are looking for greater visibility within local accounting teams to understand bottlenecks and reduce financial reporting risk.

Increased complexity is the result of numerous factors. The involvement of multiple teams—local accounting operations staff, tax, treasury, legal, corporate, and shared services organizations—creates a process with highly distributed accountability, which relies on tribal knowledge in many cases.

Through growth and acquisition, new entities and subsidiaries are rapidly emerging, creating a diaspora of acquired and legacy accounting technology. Different ERPs are left in play, which reinforces separate accounting structures and allows transactional silos to form between parties and counterparties, making it difficult to manage unreconciled balances. There also tends to be little in the way of a documentation trail.

Shared Service Centers can often reach an impasse with intercompany, struggling with a lack of visibility into subsidiary intercompany reconciliations, and facing issues reconciling transactions across different—and often relatively opaque—invoicing and receivables systems.

It all means the financial close can drag on. Or worse, corporate ends up using plugs to paper over unreconciled balances that effectively mask accounting errors and control deficiencies.

Intercompany Technology Moves to the Fore

In recent years, new technology has posed an intriguing option to cope with change. For example, one survey found that 82% of accounting and finance teams thought technology could help with pressing intercompany issues, such as transfer pricing and its surrounding compliance and documentation.[2]

Robotic Process Automation (RPA) can now use matching rules to perform intercompany matches based on tolerance levels, identifying exceptions automatically, which is ideal for managing growing intercompany transaction volumes.

An intercompany hub enables enterprises to centralize documentation, transactional details, intercompany agreements, and pricing, while acting as an ERP-agnostic connective tissue between different entities.

The meteoric rise of cloud computing also promises a side benefit for corporate and subsidiary teams: web-based access to intercompany transactions and policies from anywhere. It's naturally a better platform for cross-enterprise collaboration, rather than locking identical information behind different organizational silos and user experiences.

This CFO playbook provides you with insight into some of the most prominent trends and issues in intercompany accounting, along with common best practices implemented by global enterprises. Finally, we share an example of how one global company, Hubbell Incorporated, tackled intercompany reconciliation within subsidiaries and improved visibility at corporate.

READY FOR CHANGE →

INCREASING REGULATION & GROWING CONCERN

79% of executives describe today's international tax environment as "uncertain". [6]

RIPE FOR PROCESS REINVENTION

Just 9% of respondents indicated their company's intercompany accounting framework was "leading".[7]

TRANSFER PRICING REMAINS A BIG ISSUE

80% have experienced challenges to their transfer pricing over the past three years .[8]

Six Big Issues in Intercompany Accounting

1. Disparate Systems

Entities typically trade with each other through subsidiary-specific Purchase Order and Invoice systems. Often, it's easier to book a transaction over the phone or email, losing important documentation like proper transfer prices, currency, or appropriate taxes.

With reconciliations stacking up for the period close, it requires substantial work to balance the books, and worse, companies can accumulate write-offs that may be material.

The issue has been compounded by regular M&A activity—organizations end up with a diaspora of accounting systems, inheriting heterogeneous ERPs, charts of accounts, invoicing and payment systems, and different accounting processes.

This increases the manual effort required to complete intercompany transactions. Additionally, system complexity creates a lack of visibility between corporate and subsidiary, making issue tracing a lengthy, challenging task.

2. Intercompany Settlements & Cash Management

Challenges with intercompany settlements arise if one entity questions the correctness of an invoice, or if there are questions around differences in exchange rates or accounting periods, which must be settled to achieve balanced accounts.

Disputes often occur through email exchanges and spreadsheet attachments. This makes tracking transactions and audit trails difficult, risking compliance with government regulations and accounting standards. Organizations rely on knowledge passed down by tenured team members, which is all too easily lost when employees move on.

When intercompany accounting can't provide a clear view of approved intercompany balances to be settled, a trade imbalance typically results, which in turn impacts intercompany liquidity and FX. Unresolved intercompany positions can create unrealized gains and losses, as well as cash outflows from a tax perspective.

3. Complex Legal Agreements

Beyond typical challenges with drafting intercompany legal agreements, setting contractual terms, and meeting IRS section 482 and transfer pricing rules, legal teams face a growing regulatory environment relating to the introduction of the OECD BEPS project.

In some cases, due to weak controls and approval policies, transactions take place without legal agreements at all, exposing the organization to regulatory risk.

FAST FACTS

SPOTLIGHT ON INTERCOMPANY ACCOUNTING

OPPORTUNITY →

TOP 3 BENEFITS OF AN INTERCOMPANY UPGRADE

More efficient close and statutory reporting, improved reporting integrity, and reduction in penalties.[9]

SIGNIFICANT EFFICIENCY OPPORTUNITY

World-class organizations devote 0.8 FTEs per billion to intercompany accounting—50% less than peers.[10]

AUTOMATION ASCENDING

30% of companies are now able to automate 75% or more of their intercompany transactions and reconciliations.[11]

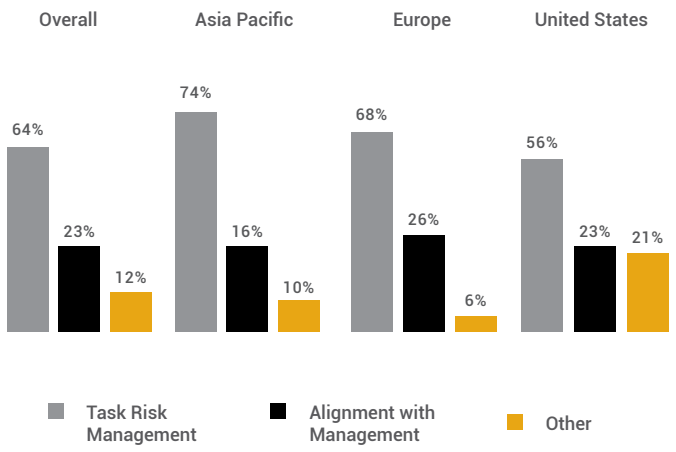
4. Transfer Pricing Compliance

Given the criticism of global enterprises' use of preferential pricing strategies to lessen their tax burden, transfer pricing is under the microscope. Failure to comply with global transfer pricing regulations can be costly, with substantial penalties incurred when tax authorities identify artificial transfer pricing.

Achieving compliance is typically a cross-functional objective across an extended chain of often-distributed internal functions and offices, with multiple hand-offs between tax, regional and global controllers, shared services, and other teams.

Risks can develop without oversight or coordination, including ambiguities in responsibility, accounting policy and data mismatches, insufficient mechanisms for reconciliation, undocumented interpretations of obtuse terms in intercompany agreements, and uncontrolled ad-hoc processes.

Drivers for Changing Transfer Pricing Policies



5. Foreign Exchange Exposure

With the increase in foreign transactions comes an associated increase in foreign currency reporting. Since many companies do business in multiple countries, this dramatically increases the complexity of reporting.

Intercompany transactions between different currencies can create and transfer risk between a reporting entity and its foreign entities, and amongst those foreign entities themselves.

Accounting teams risk misapplication of the accounting rules for foreign currency translations, and in turn, financial misstatements. Teams also often lack visibility into foreign party accounting systems and how accounts are translated.

6. BEPS Action 13

New reporting requirements for many larger international companies will require the creation of detailed country-by-country tax and financial information. In addition, a greater volume of data will need to be disclosed, dramatically increasing compliance burdens.

Companies must consider these three new levels of reporting:

- Country-by-country reporting. Details on each entity, organized by country. Data to include revenues, profits, taxes, assets, employee numbers and costs, capital, accumulated earnings, and intercompany payments. Filed in the headquarters' jurisdiction.
- Standardized information for all group members. Global organizational structure, description of business, IP development, use and transfers, intercompany financial arrangements, and financial and tax positions. Filed in each country of operation.
- Transaction details between local entities and affiliates. Local management team, business strategy, and restructurings or IP transfers. Filed in each country of operation.

SOURCE: 2019 TRANSFER PRICING AND INTERNATIONAL TAX SURVEY, EY

[1]United Nations Conference on Trade and Development
[2]*Trends in Transfer Pricing. Global Research Bulleting, Deloitte, March 2016*
[3]*United Nations Conference on Trade and Development*
[4]*Audit Analytics*
[5]*Deloitte, Poll of 4,127 accounting professionals*
[6]*EY 2019 Transfer Pricing and International Tax Survey*
[7]*Voices: The Risks of Intercompany Accounting, Accounting Today, August 2016*
[8]*EY 2019 Transfer Pricing and International Tax Survey*
[9]*Deloitte 2016, Poll of 3,800 accounting professionals*
[10]*Intercompany: The Case for Transformation, Hackett*
[11]*Ibid*
[12]*Intercompany Accounting and Process Management, Deloitte Advisory Services*

Ten Keys to Strong Intercompany Accounting

I. Centralize Data

Use a centralized Intercompany Hub to overcome the disparate ERP issue. Move toward a centralized clearing house to manage all intercompany transaction records, corresponding journal entries, statuses, supporting documents, currency rates, transfer pricing rules, and policies—all in one place.

II. Use ERP Connectors to Unify Disparate ERPs

A big issue around intercompany accounting is often the sheer number of ERPs and other systems in play. Using an intercompany solution with a rich array of pre-built connectors to typical data sources like Oracle, SAP, Sage, and Microsoft Dynamics reduces hand coding and speeds up the deployment of intercompany process centralization.

III. Standardize Policies & Procedures

Effective intercompany accounting begins with standard global policies to govern critical areas, such as data flow and stewardship, approval processes, managing charts of accounts, tax management, transfer pricing rules, currency rates, and documentation. By first centralizing, then standardizing, you'll be in a better position to, for example, assess transfer pricing documentation annually, compare it to requirements in each jurisdiction, and make centralized changes.

IV. Define & Track Workflows & Approvals

A lack of visibility into where transactions are with SSCs often frustrates BU leaders, and can cause them to begin scaling their own duplicate functional areas. Use a common platform for processing financial close tasks, reconciliations, and other areas that provide every stakeholder with a clear view on progress.

V. Consider Creating a Center of Excellence (CoE)

In unison with upgrading intercompany technology and processes, consider creating a centralized Center of Excellence that consists of stakeholders from accounting, tax, and treasury. This also ensures global standardization and orchestrated resolution of intercompany issues.

VI. Use Rules-Based Intercompany Reconciliation

Intercompany reconciliations can easily drag down local accounting teams, slowing and creating risk in the subsequent corporate close. Use rules-based matching technology to enable entity accounting teams to focus on exceptions. Technology like BlackLine can easily match transactions between one legal entity and another, and auto-certify accounts.

VII. Optimize Cash Management Processes

Forty-seven percent of organizations surveyed said they only had ad-hoc netting capabilities in place, with no defined calendar. This can lead to uncertain tax positions, and unexpected volatility in profit/loss.[12] Put a cash management strategy in place for netting and settlement around intercompany transactions. Bilateral and multi-lateral settlement on a specified calendar can help cut down bank fees, ensure better use of cash, and improve currency hedging strategies.

VIII. Sweat the Details—Be Audit Ready

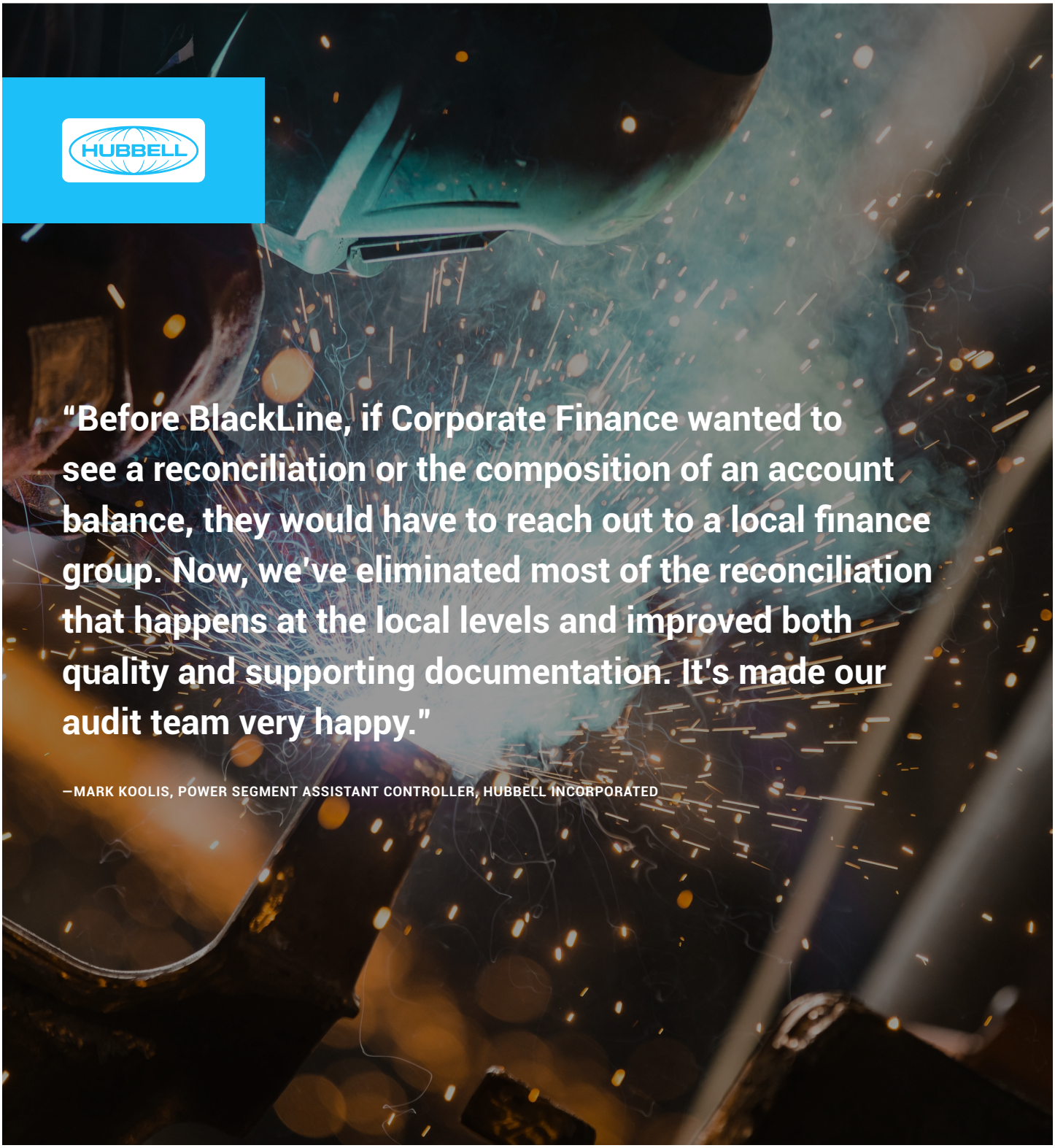
The risk of an audit around transfer pricing has never been greater. It's wise to assume the worst and be ready, especially given the often-small timeframe to respond. A centralized hub can help. But, ensure that you can drill down into specific initiator-recipient relationships to view the associated transactions. For countries that require invoices attached to intercompany transactions, use automation to ensure corresponding invoices are always attached upon final state certification.

IX. Use Cloud to Get Everyone on the Same Page

When dealing with a geographically and organizationally dispersed team, cloud computing is particularly valuable for intercompany accounting. Modern cloud applications provide an anytime/anywhere, centralized, familiar user experience for everyone—from subsidiaries to corporate—to access, update, and monitor intercompany transactions and approvals.

X. Strive for Corporate Visibility

Lack of subsidiary and intercompany visibility can be one of the biggest frustrations for corporate accounting teams and Shared Service Centers. Using an Intercompany Hub enables corporate to see where entities are in the close process without waiting hours for a report from a business unit in a different time zone or country. It also enables easy creation of reports to show balances, exceptions, and variances across entities that may impact the corporate close.



"Before BlackLine, if Corporate Finance wanted to see a reconciliation or the composition of an account balance, they would have to reach out to a local finance group. Now, we've eliminated most of the reconciliation that happens at the local levels and improved both quality and supporting documentation. It's made our audit team very happy."

—MARK KOOLIS, POWER SEGMENT ASSISTANT CONTROLLER, HUBBELL INCORPORATED

How Hubbell Incorporated Transformed Their Intercompany Processes

Hubbell is an international manufacturer of quality electrical and electronic products for a broad range of non-residential and residential construction, industrial, and utility applications. With nearly $5 billion in annual revenue, they operate manufacturing facilities in eleven countries.

Hubbell also participates in joint ventures and has sales offices in Singapore, China, India, Mexico, South Korea, and the Middle East.

Focusing on Standardization, Visibility & Automation

Effectively and efficiently managing manufacturing facilities, joint ventures, and sales offices in approximately 14 countries requires significant intercompany accounting. Before Hubbell chose to make a change, month-end close processes and day-to-day balance sheet reconciliations weren't standardized across their business units, making real-time visibility and tracking nearly impossible.

A lack of centralization for downstream, upstream, lateral trade, and non-trade intercompany transactions caused duplication, manual effort, and controls issues.

Reinventing Intercompany Accounting Processes

Hubbell selected BlackLine to standardize, automate, and simplify their close and intercompany processes. A key driver was to create robust controls and standardization across geographies and business units, while also increasing visibility.

Using BlackLine's Intercompany Hub, Hubbell implemented intercompany controls and process standardization across their business units. With automated data flows from local ledgers across 40 businesses and thousands of GL accounts, they improved reconciliation quality and supporting documentation, while reducing risk.

Self-service access to business unit intercompany accounting reports and supporting detail provided corporate with instant transparency to resolve issues, accelerate the corporate close, and simplify audits.

INDUSTRY

Manufacturing

ERP

SAP

BUSINESS IMPACT

1. Implemented strong controls and process standardization
2. Increased visibility
3. Reduced risk
4. Ensured accountants performed tasks correctly and on time

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