BlackLine
Intercompany Hub
“We had to find a better way to gain comfort in the completeness and accuracy of our financial statements.”

—JENNA STENGERT, SENIOR CORPORATE ACCOUNTING SPECIALIST, CNH INDUSTRIAL
It’s Time to Handle the Intercompany Mess

In an era of global trade, mergers and acquisitions, and increased regulations, the reconciliation and settlement of a company’s intercompany trading balances is a challenge that affects companies of every size.

Today’s organizations are far more complex than they used to be. In our global economy, accounting for intercompany transactions is no longer just an issue for large, complex organizations. It’s a consideration for fast-growing companies too.

Many organizations have significantly expanded their global footprints and are generating a spiraling volume of intercompany transactions. These challenges are complicated further by local tax policies, currencies, transfer pricing, and disparate systems and applications.

According to a report by the United Nations Conference on Trade and Development, some 80 percent of global trade takes place within the value chains of major global organizations. As volume grows, the use of spreadsheets, email or verbal approvals, or other workarounds exposes organizations to significant financial, compliance, and reputational risk.
Intercompany Transactions Defined

Intercompany transactions happen when one entity is involved in a transaction with another entity within the same organization. Common scenarios include accounting for intercompany sales and purchases between a parent company and its subsidiaries. It also includes fee sharing, cost allocations, royalties, and financing activities.

If these kinds of transactions are improperly accounted for in either entity, any out-of-balance accounts can seriously impact financial statements, creating compliance issues, risk of restatement, SEC imposed fines, and shareholder lawsuits.

So where does this leave most organizations?

The intercompany accounting process is most often handled through labor-intensive manual processes with detective instead of preventative controls in place. It is not uncommon for large multinational corporations to have hundreds of staff only handling intercompany transactions.
Intercompany Stakeholders

**Accounting**

The accounting organization is focused on mitigating the primary risk of improper intercompany accounting—financial misstatements—which can carry substantial risk to reputation and erode shareholder value. Typically, this can mean significant manual effort to document, reconcile, net, and settle intercompany transactions. It can expose the organization to an inefficient and lengthy close and to weaknesses in internal controls that may surface during an audit.

**Treasury**

Managing the netting and settlement of intercompany trade is one obligation of Treasury. Often, Treasury does not have the transactional detail they need, due in large part to disparate sources and posting systems in which the transactional data resides. This can hinder the Treasury Department’s ability to accurately net and settle intercompany accounts. The inability to provide treasury teams with approved intercompany balances for settlement creates trade imbalances, which in turn impacts intercompany liquidity and foreign exchange exposure.

**Tax**

Among other responsibilities, tax functions are focused on ensuring that transactions between countries meet specific tax laws and compliance, and that they’re not misclassifying profits between countries that expose the organization to risk. Constantly shifting tax landscapes present significant challenges, such as legislation for country-by-country reporting around Base Erosion and Profit Shifting (BEPS). Tax functions must now support transparent financial statements for individual countries, allowing for the easy identification of country-level financials.

**Legal**

Intercompany transactions create complexity for legal teams. They must ensure transactions comply with local legal requirements, and manage the allocation of risks and responsibilities, ownership of intellectual property, and guidelines for tax compliance audits. They must also craft agreements to support Section 482 requirements—the arm’s length standard for how taxpayers determine their true taxable income as it relates to intercompany transactions.
The belief that everything nets to zero has been replaced by the realization of the risks and costs hiding within the end-to-end intercompany accounting process. Managing intercompany transactions is labor-intensive and costly. In addition to handling volume and checking and tracing errors to mitigate risk, the process is also often hampered by limited visibility into foreign party systems. Because intercompany accounting is highly distributed, there are fewer controls and lower accountability.

Most intercompany issues are discovered during the period-end close, in financial reporting and account reconciliation processes. Cumulatively, they can drain valuable accounting and finance resources, create redundant work and outstanding balances, and elevate exposure to risk. In fact, per Audit Analytics, intercompany issues were the fifth highest reason for restatement between 2001 and 2016.

In a 2016 survey by Deloitte of over 3,800 accounting professionals, nearly 80% experienced challenges with intercompany accounting around disparate software systems within and across business units and divisions, intercompany settlement processes, management of complex legal agreements, transfer pricing compliance, and FX exposure.
## Restatements by Reason

<table>
<thead>
<tr>
<th>Reason</th>
<th># of Restatements</th>
</tr>
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<tbody>
<tr>
<td>Debt, quasi-debt, warrants &amp; equity (BCF) security</td>
<td>2,500</td>
</tr>
<tr>
<td>Expense (payroll, SGA, other) recording</td>
<td>3,000</td>
</tr>
<tr>
<td>Revenue recognition</td>
<td>O</td>
</tr>
<tr>
<td>Acquisitions, mergers, disposals, re-org acct</td>
<td>O</td>
</tr>
<tr>
<td>Foreign, related party, subsidiary, intercompany</td>
<td>O</td>
</tr>
<tr>
<td>Deferred, stock-based and/or executive comp</td>
<td>O</td>
</tr>
<tr>
<td>Liabilities, payables, reserves and accrual estimate</td>
<td>O</td>
</tr>
<tr>
<td>Tax expense/benefit/deferral/other (FAS 109)</td>
<td>O</td>
</tr>
<tr>
<td>Cash flow statement (SFAS 95) classification errors</td>
<td>O</td>
</tr>
<tr>
<td>PPE intangible or fixed asset (value/diminution)</td>
<td>O</td>
</tr>
<tr>
<td>Accounts/loans receivable, investments and cash</td>
<td>O</td>
</tr>
<tr>
<td>Inventory, vendor, and/or cost of sales</td>
<td>O</td>
</tr>
<tr>
<td>Consolidation incl Fin 46 variable interest &amp; off-B/S</td>
<td>O</td>
</tr>
</tbody>
</table>

*SOURCE: AUDIT ANALYTICS*
Intercompany Accounting Challenges

Intercompany accounting is notoriously a convoluted process which can involve multiple technology systems between trading entities. Often, it’s easier to book the transaction over the phone or email, but in the process, you lose important documentation like proper transfer prices, currency, or appropriate taxes. With reconciliations stacking up for the period close, this often creates substantial work to balance the books, or worse, causes write-offs that may accumulate to be material.

The issue has been compounded by increased merger and acquisition activity. Organizations have often ended up with different accounting processes, increasing the manual effort required to complete intercompany transactions. In turn, systems complexity creates a lack of visibility between corporations and subsidiaries. As a result, tracing the issues becomes a lengthy, challenging task.

With the growth of organizations, shared services functions often take shape. This puts a significant burden on the centralized function to chase down, collect, and reconcile intercompany transactions conducted between parties—elevating the risk of write-offs.

Intercompany Settlements
Challenges with intercompany settlements often arise if one entity questions the accuracy of an invoice, or if there are questions around exchange rate discrepancies or different accounting periods that must be settled to achieve balanced accounts. Disputes between the two parties often lead to after-the-fact email exchanges and spreadsheet attachments, complicating the tracking of transactions and audit trails, increasing the amount of time required to reconcile the affected accounts, and risking non-compliance with government regulations or accounting standards.

Complex Legal Agreements
Beyond the typical challenges of drafting intercompany legal agreements and setting contractual terms, and meeting IRS section 482 and transfer pricing rules, legal teams face a growing regulatory environment with the introduction of the Organization for Economic Cooperation and Development (OECD) BEPS project. In some cases, transactions take place without any legal agreements due to weak controls and approval policies, exposing the organization to regulatory risk.
Transfer Pricing Compliance

Transfer pricing compliance is generally the domain of a senior tax manager, but execution is typically a cross-functional task. It is spread out 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. Without oversight or coordination, risks can develop, including ambiguities of responsibility, accounting policy or data mismatches, insufficient mechanisms for reconciliation, undocumented interpretations of ambiguous terms in intercompany agreements, and ad-hoc, uncontrolled processes.

Foreign Exchange Exposure

With the increase in foreign transactions comes an associated rise in foreign-currency reporting, and since many companies do business in multiple countries, this dramatically heightens the complexity of reporting. Intercompany foreign currency transactions can create and transfer foreign currency risk between a reporting entity and its foreign entities, and among the foreign entities. Accounting teams face misapplying the accounting rules for foreign-currency translations. Misstated financials often lack visibility into foreign party accounting systems and how accounts are translated.
Why Now? Regulators Turn up the Heat.

Regulatory authorities worldwide have noticed the trend in the growing corporate global footprint and exploitation strategies being used for tax avoidance. As a result, new regulations and strict enforcement of intercompany accounting practices are consistently appearing.

**BEPS Tax Regulations**

New Base Erosion and Profit Shifting tax regulations, formulated by the OECD and published in October 2015, spurred the most significant changes to the taxation of international business since the 1980s. The countries directly involved in the OECD BEPS project make up over 84 percent of the total world economy, and per PwC, 70 percent of CFOs are concerned about increasing tax burdens from the new regulations.

Intercompany transactions, including sales, loans, and licenses, play a significant role in multinational global operations. BEPS is focusing on these transactions, modifying the value attributed to rules and the types of arrangements that will be respected. Many companies use ‘hybrid’ transactions, involving companies or instruments that are treated differently in the various tax jurisdictions, often resulting in tax benefits. With the introduction of BEPS, these kinds of transactions will likely be subject to more restrictive treatment by some jurisdictions in the future, which may result in double taxation or otherwise affect the profitability of certain intercompany transactions.

New reporting requirements for many larger international companies will require the creation of detailed country-by-country tax and financial information. In addition, it will call for a greater volume of data to be disclosed, dramatically increasing compliance burdens. In fact, companies must consider 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
- Financial and tax positions
- Intercompany financial arrangements
- Filed in each country with operations

Transaction Details Between Local Entities & Affiliates

- Business strategy
- Restructurings or IP transfers
- Filed in each country with operations

What BEPS Means for Systems & Processes

With greatly increased needs for data and reporting, BEPS will place substantially increased pressure on systems and personnel. This burden will require well-organized document management, data, and workflow systems to increase collaboration across tax, finance, and geographies. Multinationals face the practical requirement of reconciling public financial statements, legal entity books, local tax returns, and templates.

Public Company Accounting Oversight Board: Auditing Standard 2410

The PCAOB approved a new standard on auditing transactions with related parties. The standard requires auditors to understand and evaluate the company’s process to identify, authorize, approve, account for, and disclose related party relationships and transactions. Auditors must evaluate whether the obtained evidence supports or contradicts a management assertion in the financial statements. They also need to determine that transactions with related parties were conducted on the same terms as arms-length transactions.

What PCAOB Auditing Standard 2410 Means for Systems & Processes

To meet the new requirements, companies should review the processes and controls they have in place to identify, account for, and disclose related party transactions—a significant challenge if they are buried under spreadsheets and other documents. To meet some of the new requirements, auditors will often need assistance. For example, any related party transactions that require financial statement disclosure or represent a significant risk, and do not have strong processes, may extend audit cycles.
Benefits of Intercompany Automation

- 16.5% Don’t know
- 5.6% A more reliable internal control environment
- 3.1% Reduction in fines, penalties, etc.
- 13.2% Financial reporting integrity
- 21.4% More efficient close & statutory reporting process
- 40.2% All of the areas

Source: Deloitte 2016, Poll of 3,800 accounting professionals
## Ten Point Self-Assessment of your Intercompany Accounting Processes

<table>
<thead>
<tr>
<th>Intercompany Issue</th>
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<tbody>
<tr>
<td>1. Significant volumes of transactions and staff time</td>
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<td>2. Manual transaction creation or approval</td>
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<td>3. Multiple systems where transactions are entered</td>
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<td>4. Intercompany write-offs</td>
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<tr>
<td>5. Lack of visibility into the underlying transactions at the consolidated level</td>
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<td>6. Lack of clarity around transfer pricing policies and procedures</td>
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<td>7. Manual processes for currency translation and conversion</td>
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<td>8. Frequent out of balance intercompany transactions</td>
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<tr>
<td>9. Email and lack of documentation for approval from both parties</td>
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<td>10. Invoices not linked to intercompany transactions when required</td>
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</table>

**TOTAL NUMBER OF INTERCOMPANY ISSUES:**   
BlackLine Intercompany Hub: Reduce Risk, Embed Controls, Increase Efficiency

BlackLine’s Intercompany Hub delivers what finance and accounting leaders have been looking for: an end-state structured intercompany technology solution. It provides automation, workflow, and documentation that increases the speed and efficiency of the financial close, strengthens controls, increases confidence, and reduces risk.

Technology platform agnostic, Intercompany Hub’s cloud-based platform connects to any ERP system to ensure data flow across the enterprise. Powerful automation and documentation improves an organization’s ability to book intercompany transactions and reduces the risk of write-offs.

Organizations report significant benefits from automating and streamlining intercompany processes, including a more efficient close, stronger financial reporting integrity, and reduction in risk.

The results of achieving a best-in-class approach can be substantial, and intercompany accounting has one of the largest disparities between the efficiency of world-class and average finance organizations. In fact, according to a 2015 research piece by The Hackett Group, Intercompany Accounting – The Case for Transformation, world class organizations have half as many FTEs per billion dollars of intercompany revenue.
The Path to Intercompany Transformation

Intercompany Hub is a technology solution that can address the most complex organizational intercompany accounting needs. The software has the capability to handle large volumes of transactions, with structured workflow, in a central repository to build efficiency, cost savings, and repeatability into organizations. This establishes a solution that is implementable, measurable, and ensures organizational success.
Centralize Global Governance & Policies

Effective intercompany accounting begins with standard global policies governing critical areas, such as entity trading hierarchy, data flow and stewardship, approval processes, managing charts of accounts, tax management, transfer pricing rules, currency rates, and documentation.

Ensuring a centralized hub for stakeholders from accounting, tax, and treasury to provide global standardization and a platform for organized resolution of intercompany issues.

**How BlackLine helps:**

- Governance of intercompany entity relationships and trading hierarchies
- Centrally store and enforce documents such as chart of accounts, transfer pricing agreements, and allocations
- Provides a single system from which transactions are initiated, approved, validated, and booked
- Establishes easily manageable permissions and restrictions on intercompany trading
- Quickly link to related transactions, reconciling items, and supporting documentation
- Ensures pre-approval on both sides of the transaction prior to executing
- Develops configurable fields and calculations to handle business change
A significant challenge for global organizations is disparate finance and accounting systems, often because of M&A or the launching of new businesses. A sustainable approach to integrating multiple ERP systems ensures that new and acquired accounts are set up in alignment with policies—data flows out of them into intercompany workflows, and intercompany transactions are processed in a standardized way—not dependent on opaque rules embedded in the underlying ERP.

**How BlackLine helps:**

- Creates one integrated repository for all data
- Controls the creation of intercompany transactions with standard templates
- Automatically creates both sides of the transaction between trading entities
- Dynamic workflows route transactions to appropriate individuals based on business rules or entity hierarchy
- Pre-posting validation eliminates entry errors
- For countries that require invoices, automatically creates and attaches them to transactions
- Provides a centralized, familiar user experience from subsidiaries to corporations, with clear visibility to intercompany transactions using an intercompany grid
Automated Intercompany Matching & Reconciliation

BlackLine provides automated transaction matching and intercompany reconciliation from multiple data sources to reduce effort and enable accounting to focus on exceptions.

How BlackLine helps:

- Matches intercompany transactions automatically to external data sources
- Frees accounting to focus on exceptions with rules-based matching functionality
- Manages any accounting transaction type, including:
  - Bank to General Ledger
  - Bank to Credit Card
  - Bank to Accounts Receivable
  - Received Not Invoiced to Invoice Received
  - Third-Party Invoices to Internal Records
  - Intercompany Transactions
  - Investment Transactions
- Creates reconciling items as part of a reconciliation
- Includes a direct link to incorrect transactions within a correcting journal entry
- Stores all transactional level detail in one place
Netting & Settlement Facilitation

Compliment treasury management system capabilities with global settlement views. Bilateral netting reduces the number of transactions required for settlement between entities.

How BlackLine helps:

- Summarizes settlement details to enhance visibility of the end-to-end intercompany process
- Displays net payees and net payors within the organization
- Drills down into specific trading partner relationships to view the associated transactions
- Automatically imports foreign exchange rates
- View net-eligible versus non-net-eligible transaction amounts across transacting entities
Hubbell Modernized with BlackLine.

“With BlackLine, we’ve automated much of the financial process and enhanced our quality and supporting documentation. It’s made our audit team very happy.”

—MARK KOOLIS, POWER SEGMENT ASSISTANT CONTROLLER, HUBBELL INCORPORATED
Proof of Success: Hubbell

Hubbell Incorporated 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 2015 revenues of $3.4 billion, Hubbell Incorporated operates manufacturing facilities in eleven countries. Hubbell also participates in joint ventures and has sales offices in Singapore, China, India, Mexico, South Korea, and countries in the Middle East.

The Challenge

Effectively and efficiently managing global manufacturing facilities, joint ventures, and sales offices requires real-time access to all financial metrics, including intercompany activity, reconciliation completion status, and quality ratings.

Hubbell’s downstream, upstream, and lateral trade and non-trade intercompany transactions were not centralized across legal entities, causing duplication and manual work efforts, lack of enforcement of cross-company transactions, and foreign exchange rates confusion.

The Solution

Hubbell chose BlackLine to standardize, automate, and simplify the close and intercompany processes while simultaneously increasing visibility. Strong controls and standardization across geographies and business units were key drivers.

The Results

- Implemented strong intercompany controls and process standardization across multiple business units, regardless of location, language, or currency
- Reduced tax and compliance risk by automating intercompany journal entries, booking both sides of the transaction automatically in the correct currency, providing real-time posting and validation in SAP
- Increased visibility into where they are in the close process without waiting hours for a report from a business unit in a different time zone or country
The Future of Accounting & Finance

BlackLine is modernizing finance to inspire greater productivity and enable the detection of accounting errors before they lead to devastating financial restatement.

BlackLine’s Intercompany Hub furthers this mission by allowing companies to perform real-time and continuous analysis of global intercompany accounting. It streamlines and automates intercompany transactions, and presents CFOs and Controllers with the information they need to know, such as who owes whom in the organization at any given moment, while enabling the monitoring of trends across global currencies.

Intercompany Hub empowers customers with multiple entities to streamline time-consuming intercompany reconciliations, as well as inter-entity journal posting, netting, and settlement functions. It eliminates complex, disjointed accounting tasks, provides unprecedented global visibility, and empowers finance and accounting organizations to work smarter, not harder. It fills in the gaps left by ERP systems to create a more efficient intercompany process and a competitive advantage for leaders newly equipped with data-driven intelligence. Ultimately, it embeds a streamlined and automated intercompany process that not only improves efficiency, but also ensures integrity so you can trust the balance of your intercompany accounts.
BlackLine is a provider of cloud-based solutions for Finance & Accounting (F&A) that centralize and streamline financial close operations and other key F&A processes for midsize and large organizations. Designed to complement the ERP and other financial systems, the BlackLine Finance Controls & Automation Platform increases operational efficiency, real-time visibility, control and compliance to ensure end-to-end financial close management, fueling confidence throughout the entire accounting cycle.

BlackLine’s mission is to continuously improve the quality, accuracy, and efficiency of Accounting & Finance by centralizing key accounting functions within a single, unified cloud platform. BlackLine enables customers to move beyond outdated processes and point solutions to a Continuous Accounting model, which embeds real-time automation, controls, and period-end tasks within day-to-day accounting activities. As a result, BlackLine helps companies achieve Modern Finance and ensures an efficient and more accurate financial close. More than 2,000 companies around the world trust BlackLine to ensure balance sheet integrity and confidence in their financial statements.