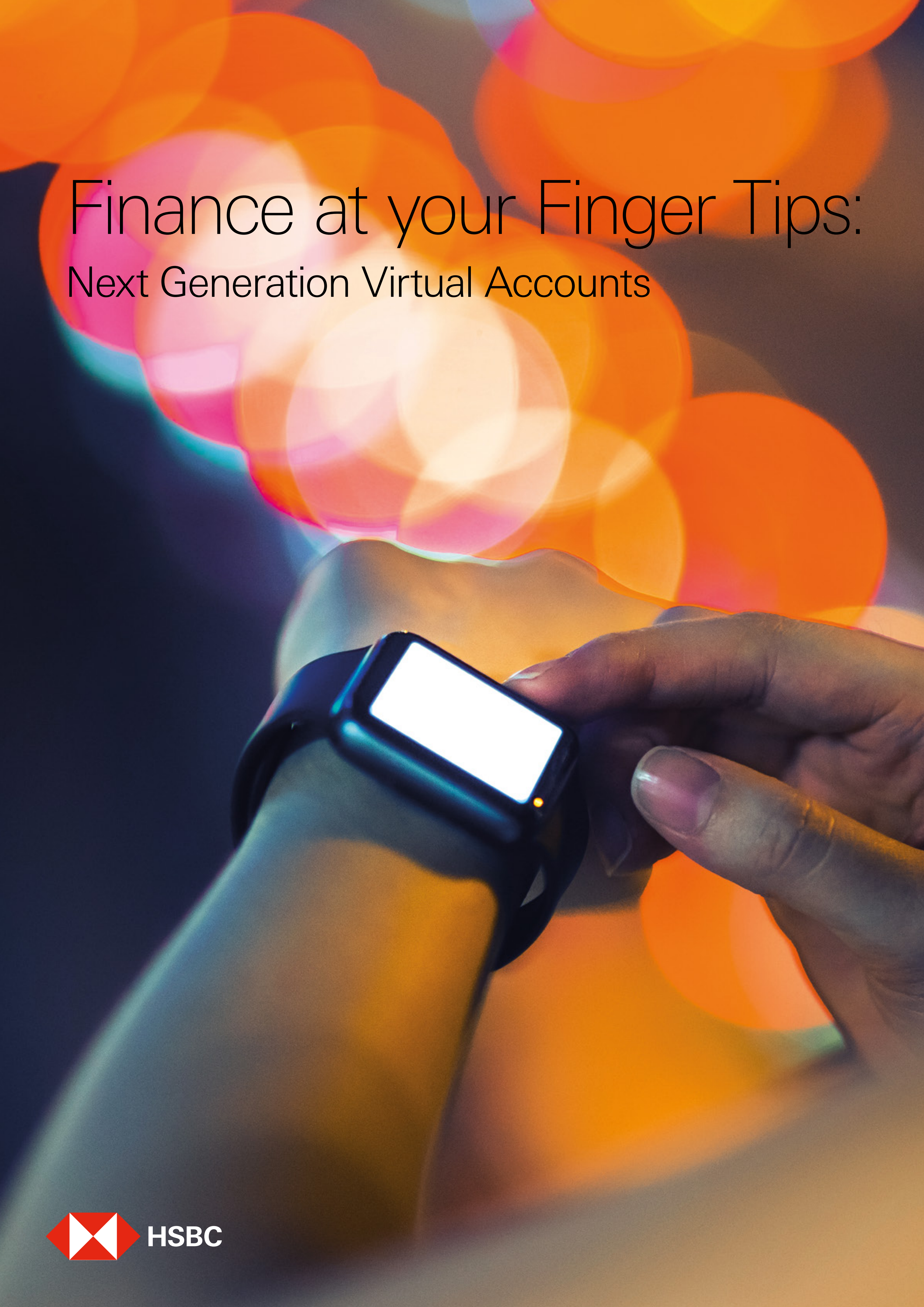
Finance at your Finger Tips:

Next Generation Virtual Accounts



HSBC

Finance at your Finger Tips: Next Generation Virtual Accounts

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Virtual accounts are not a new concept, but in their most recent incarnation as HSBC's next generation virtual accounts (ngVAs) they add a number of important additional benefits for corporate treasurers. Timothy Bartlett, Senior Commercialisation Manager, Liquidity and Investments at HSBC explain how ngVAs can quickly and substantially enhance visibility, control, centralisation and liquidity management.

Virtual accounts have long been used as a solid method for improving the quality of accounts receivable reconciliation, whereby receivables from particular customers can be allocated to specific virtual accounts. This gives accounts receivable teams certainty on the precise identity of the payee. This is a significant improvement on the current situation for many corporates, where multiple customers may be sending remittances to the same physical account, with remitter details possibly being incomplete (or truncated by the clearing system).

Easier administration

HSBC's ngVAs, which are currently available in the UK with roll out in further jurisdictions planned, add better administrative control with several additional functions and advantages. Historically, much of the administration of virtual accounts (such as the creation of new virtual accounts) has had to be undertaken on behalf of clients by their banks. In the case of HSBC ngVAs, an important element of self -service has been added, to support faster deployment and more convenient control of the virtual accounts.

ngVA functionality is accessible via HSBCnet, where clients can request an allocation of virtual accounts to sit beneath a physical account. From a financial crime compliance perspective, HSBC will conduct full Know Your Customer (KYC) on the entity holding the physical account. If the virtual accounts beneath this physical account are allotted to different entities, then less onerous due diligence requirements will be applied to these - though substantive oversight will still be applicable.

An important benefit is that once these ngVAs are allocated by the bank, clients can activate them as required. Once this is done and the appropriate ERP[1] configuration made, any subsequent movements over the virtual accounts are automatically reflected in the entities' ledger records in the ERP system.

POBO/ROBO

ngVAs can also facilitate in-house banking, because centralised processes - such as payables on behalf of (POBO) and receivables on behalf of (ROBO) - can be made considerably easier and more efficient through their use.

In the case of POBO, in order to ensure sufficient payment transparency, payments originating from an HSBC ngVA will appear to originate from the 'parent' physical account. However, the underlying payer details will still be accessible in payment messaging, so larger beneficiaries with treasury or enterprise resource planning systems should still be able to auto-reconcile the remittances.

Therefore, a client's treasury centre might operate relatively few physical accounts denominated in various currencies. For example, beneath each physical account could be a set of ngVAs, denominated in the same currency as the physical account, with each ngVA assigned to a different business entity or country of operation. The segregation provided by the virtual accounts ensures traceability and transparency, while at the same time simplifying the process of making payments under a POBO model. Very similar advantages apply in the case of ROBO, so if treasury is operating both POBO and ROBO, each physical account might have two ngVAs per entity beneath it, one for the entity's payables and one for its receivables. (Although in practice each entity might have multiple virtual accounts for receivables, one for each of its customers.)

ngVAs are also scalable, so the benefits outlined above are also accessible in a high volume retail environment. For example, a real estate company might choose to allocate ngVAs to all its tenants or a retail store might choose to allocate an ngVA to each department, or even each cash till.

[1] Enterprise Resource Planning

Liquidity management

Changes implemented under Basel III have created significant changes relating to the regulatory capital banks must hold against specific activities or products. A case in point is notional pooling, where increased capital costs have made them a less straightforward proposition.

Happily, this is an area where ngVAs can fulfil a very similar function. Each entity's liquidity is held in a virtual account, but is still completely transparent from a treasury perspective, while still maximising liquidity management performance. Furthermore, using HSBCnet, treasuries are able to view all physical and virtual accounts across currencies and geographies for a completely global view.

However, ngVAs are not an exact replacement for notional pooling because by definition they effectively co-mingle funds and create a net intercompany position. If this is of concern, a notional pool remains a better alternative.

Reducing costs and use with existing solutions

ngVAs also have a number of ancillary benefits. As they are actually ledger records, not real bank accounts, the costs associated with operating them are lower than for physical accounts. Furthermore, because any transactions sent to/from ngVAs have to go via their parent physical accounts, they can still be used for many of the activities associated with physical accounts.

For instance, if treasury has set up automated FX transactions with its bank at a pre-agreed spread for an entity's physical bank account, that arrangement would still be equally valid if the entity's account were virtual rather than physical. By the same token, virtual accounts can also participate indirectly (via the physical account) in a notional pool or a cash concentration structure.

Conclusion

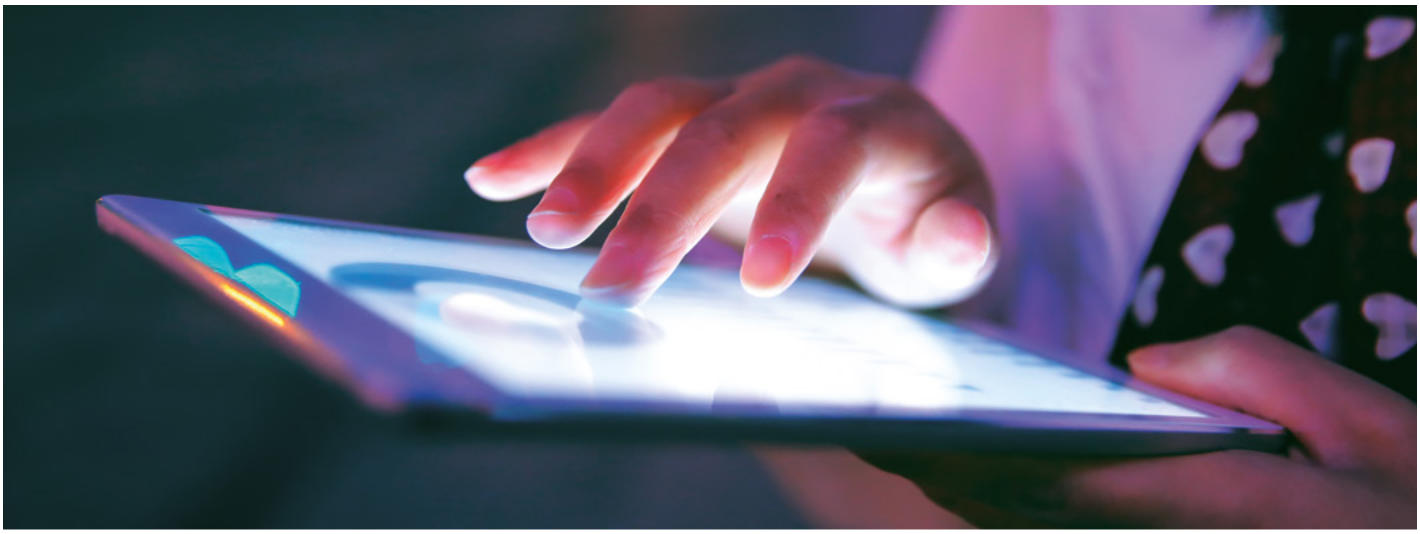
ngVAs build upon the existing reconciliation benefits of ordinary virtual accounts in a number of important ways, many of which are interconnected and complementary. The bottom line is that they offer clients valuable opportunities to improve efficiency, ranging across automation, centralisation, transparency and efficiency.

Allocated and published virtual accounts

Virtual accounts are available in two basic forms: allocated and published.

Allocated: a typical example of an allocated virtual account would be a lawyer's client money account, where each client's funds are assigned to a specific virtual account and labelled accordingly. However, allocated virtual accounts like this are not intended for external use, such as receiving remittances from third parties directly, so they do not have account numbers and sort codes recognisable by clearing systems.

Published: by contrast a published virtual account will have an IBAN that conforms to the convention of the location of the physical account. For instance, if the parent physical account is based in the UK, then the underlying virtual accounts will each have their own unique IBAN, consisting of the branch sort code and an eight digit account number. This means that published virtual accounts are recognised by clearing systems, so payees can remit directly to them using the IBAN details.



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