

# Repatriating Cash to the US from India

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"Country roads, take me home... to the place I belong". When John Denver crooned these immortal lyrics, he could have been singing for the dollars lying in the overseas subsidiaries of US corporations. Can the greenbacks in Indian subsidiaries also sing this tune?

The rapidly expanding economy in India has traditionally seen only a one-way movement of capital – which is into the country. However, there is an undercurrent of interest among local Indian subsidiaries of US tax-paying corporations on how they can contribute to their parent's HIA (Homeland Investment Act) opportunity. This is especially true for US tax-paying corporations with Indian subsidiaries that are past the investment phase and are looking at options to redeploy their current profitability outside India. India is a possible source of dividends for repatriation.

Following is a framework of the local regulatory, tax and financial services to achieve the corporation's HIA objectives. Keep in mind the fact that there are local challenges in the planning, execution and post implementation phases that must be managed carefully. It is critical to have a banking partner embedded in India to provide advice on the local banking framework's possibilities and limitations for a smooth "ride back home".

## "Can we do it?" – Understanding the regulatory framework

Indian companies must work closely with their American parents to determine if they are the best source for HIA-related

dividends. In general, dividends will come from subsidiaries with not only excess profits but also limited local reinvestment opportunities and flexible country regulations. Marginal tax rates are also important. These topics are beyond the scope of this article, but the Indian regulatory climate is generally flexible and subsidiaries can pay dividends with few restrictions. Some of the issues are discussed below.

After the analysis of earnings and local investment options, the first step for corporations is to consider the four major laws to help evaluate the regulatory permissibility and extent of dividends they can pay:

**Companies Act**, which governs the general corporate framework and the approvals required for declaration and payment of dividend:

- Dividends are paid out of profits adjusting for depreciation and previous losses
- Restrictions are on usage of the general reserves for payment of dividends
- Dividends typically need to be paid equally to all shareholders within a class
- There are timelines for payment after the declaration of dividend and treatment of unpaid/unclaimed dividends.

There are also rules governing the frequency of payments including how to treat interim and final payments.

**FEMA (Foreign Exchange Management Act)**, defines permissibility, documentation and CPA certifications required to support the remittance to non-resident stakeholders:

- Allows hedging of the exposure created by the dividend but only after declaration of the dividend

**SEBI (Securities Exchange Board of India)** and Stock Exchange guidelines for listed companies to handle investors' funds and book closures/record dates:

- Process for disclosure of declaration of dividends to Stock Exchanges.

**The Indian Income Tax Act** and related guidance, where the dividend income is typically subject to a dividend distribution tax that is paid by the dividend-paying corporations prior to disbursement:

- There is a Double Tax Avoidance Treaty between India and the United States and some other countries where holding corporations are incorporated allowing for benefit of this tax to be utilised
- Extinguishment of capitalised retained earnings can be treated as dividends under the Income Tax Act
- There is no further tax deducted for dividends repatriated overseas.



Taj Mahal, India

Of course, the foregoing review of regulations only illustrates the potential complexity of the dividend process. Each company must also interpret these regulations based on its own facts and circumstances.

**"Do we have the funds?" – Arranging and managing the liquidity prior to repatriation**

Local laws as well as the American Job Creation Act 2004 require the HIA repatriation dividend to be paid in cash; corporations may need to look at raising funds if their repatriation targets permissible under regulations exceed current cash surpluses.

Historically, the government required multinational companies to include local equity ownership in the capital structure, resulting in potentially numerous local shareholders. A large local shareholding may significantly reduce the cash flow and tax benefit available to the US tax-paying corporation. A meaningful dividend from a HIA perspective could have a significant drain on the cash and net worth positions of these corporations.

There are a variety of options for raising funds. Most of these are tactical in

nature to meet the immediate objectives of raising cash as opposed to structural. Options for raising funds include:

- Balance sheet optimisation through sale of receivables, which additionally improves their day's sales outstandings as well as economic value added. Banks operating in India can provide several structures
- Asset sales and lease-backs to free up blocked cash value for core assets
- Movement of employee loans, vehicle advances, housing loans, etc. from the corporation's balance sheet to commercial bank supported structures
- Capital re-structuring solutions to absorb free cash into the holding corporation or issue of debentures
- Short-term borrowings.

Due to the lead time between raising funds and dividend declaration and repatriation, corporations with surplus cash will be looking at planned maturity

and short-term investment solutions to optimise return on their idling balances. Some of the investment options include:

- Banking deposit products for both actively and passively managed sweep products
- Money market and debt mutual funds
- Deposits with other corporations or investments in their commercial paper
- Local sovereign debt
- Temporary payments to suppliers to earn cash discounts that frequently 'earn' a return greater than other short-term investments.

**"How do we manage the dividend process?" – The execution process**

If a publicly held corporation decides to make a dividend, it needs to pay dividends to all shareholders in the same class in proportion to their equity holdings in that class. This dividend payment is a cumbersome task for

some of the US corporations in India which, due to historical limits on foreign investments, have significant public holdings. The key challenges flow from a decentralised cash clearing system and regulatory procedures as below:

- The most frequent payment mechanism for dividends is paper, a logistics nightmare that poses the threat of fraud and forgery
- Handling a large number of checks is a challenge for both making the payment instruments as well as mailing to various parts of the geographically dispersed country
- Investors require local 'payable at' locations that usually include over 100 cities and towns – which may require partnering with multiple banks
- Extensive reconciliation is required for regulatory reporting
- Non-resident holdings require payments made in multiple currencies.

To overcome these hurdles, most companies in India have successfully outsourced their dividend payment process to leading cash management banks with the technological infrastructure and local tie-ups to support these payments. These banking partners can smoothly make timely, bulk payments

with fraud prevention tools to any number of investors.

### "How do we manage my cash balances now?" – Post repatriation liquidity management

Once the immediate need for cash has passed, companies may require more structural changes in balance sheet organisation. For the savvy corporate treasurer, these changes are not expected to be a serious concern today, due to the alternatives available in the Indian economy.

Some corporations evaluating significant repatriation for HIA are trying to develop efficiencies in their cash management process to improve availability of funds and information to address their working capital funding drags. Discussions with bankers have ranged from up-tiering their receivables management processes via banking partner consolidation, to improved information reporting and funds flow across multiple banking partners. Solutions for automated daily concentration between banks or improved daily reporting or balance aggregation are critical. To reduce cash gaps not addressed via internal processing efficiencies, some corporations have initiated discussions on various debt options. Most solutions are currently economically priced in India due to a stable country risk rating and excess liquidity in the financial system for quality borrowers.

If used judiciously, the solutions below

will allow corporations to introduce foreign currency debt in their balance sheet and hence take advantage of INR (rupee) appreciation against some currencies. Additionally, some corporations are looking to realign capital distribution in their balance sheet and improve leverage – and hence shareholders' return on equity. Some of the more structural options include:

- Borrowings through commercial paper and certificates of deposit
- External commercial borrowing from outside India
- Term funding via Indian rupee or foreign currency debt
- Re-negotiation of supply chain trade terms to permanently decrease working capital gap.

Corporations may also consider other funding options such as domestic or overseas equity issues, but they are not expected to be popular as there are concerns around ownership dilution and they may be governed by sectoral industry investment caps in the country.

Overall, the Indian corporate and financial framework can support dividend repatriation to meet US corporations' HIA objectives. Execution is key, however, and requires careful planning and partnering with reliable advisors and bankers in India. ■

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