Expansion pack

RANA FAYEZ EL-HAJJAR EXPLAINS HOW THE TREASURY DEPARTMENT AT QATARGAS MET THE CHALLENGES OF A HUGE LNG EXPANSION.

Set up in 1984, Qatargas pioneered the liquefied natural gas (LNG) industry in Qatar, with three LNG trains designed to produce six million tonnes a year. By the end of this year, the company will be operating seven LNG trains (the liquefaction and purification facilities in an LNG plant) and exporting more than 42 million tonnes of LNG a year to markets in Europe, Asia and North America.

This exponential increase in volume has been made possible thanks to the largest LNG trains and ships ever built. It was a mega vision that posed mega challenges for everyone in Qatargas, and treasury was no exception.

EXPANSION To support the expansion, Qatargas treasury needed to manage the corporate governance of seven legal entities with nine different shareholders and a host of shared facilities. This demanded detailed knowledge of the treasury implications of numerous and voluminous joint venture, fiscal, facilities sharing and service agreements.

Some shareholders had varying asset ownership interest within the same legal entity. Taking into consideration the volume of cashflows associated with single sales transactions, Qatargas had to identify the cashflow streams associated with the asset owned and ensure that payouts to the shareholders reflected their ownership of cash generated from that asset.

Treasury was also responsible for administering a loan portfolio for the various joint ventures in excess of $14bn. These project finance loans came with their own stringent loan covenants, multiple cash waterfalls and very demanding financial completion requirements, all of which needed to be managed uniquely for each entity.

And once the gas started flowing, managing cash became a real challenge. Investment management – an activity previously handled alongside other treasury work – had to become a full-time job.

Moreover, with Qatargas becoming an active player on the global LNG market, the counterparty credit risk associated with sales needed to be actively managed.

Qatargas also had to manage multiple local and international banking relationships, making bank account administration especially cumbersome because of the number of legal entities involved.

Insurance was especially complicated. With the commencement of the mega trains construction in 2004, the volume of work and its complexity increased significantly to respond to the needs of four separate onshore and offshore ventures. Each of these ventures had different shareholders but at the same time share common facilities with different ownership interest. The actual procurement of the insurance had to meet very stringent loan compliance obligations. Qatargas was eventually handling one of the largest single insurance programmes in the world, dealing with local insurers, international insurance brokers and lenders' insurance consultants.

MAJOR RESTRUCTURE Treasury management in the days of the first three LNG trains had been relatively simple, with a limited number of staff, many of whom managed the daily operations through multitasking. This simple operation had to undergo a major restructuring exercise very quickly to keep up with the pace of the expansion activities.

The most critical first step was to reorganise treasury staff into four functional areas: cash management, treasury operations, loan compliance and insurance. This specialisation paved the way for the necessary system and process changes and allowed for increased segregation of duties in a very high-risk environment.

The cash management group handled the daily cash

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management and investment activities in line with the cash waterfall mechanisms imposed by the lenders. They took care of bank account administration and relationship management for each of the ventures' local and international account banks and investment counterparties. This group was also responsible for administering the monthly cash distributions to the shareholders of the various ventures according to the specific requirements of each joint venture agreement.

Soon after they were set up, the cash management and compliance groups took the lead in working with the company's enterprise resource planning (ERP) consultants to determine the treasury-related business requirements and conceptual design for each of the ventures complied with the joint venture agreements as well as the lenders' requirements.

The treasury operations group took care of the back-office function, in addition to financial and credit risk management for all the ventures. This group also controlled all electronic banking systems and identified the adequacy of internal controls within the whole of treasury.

The loan compliance group was responsible for ensuring compliance of each of the ventures to their financing obligations with the lenders, including loan drawdowns, owner cash calls, regular reporting, and the onerous responsibility of co-ordinating financial completion requirements for all the LNG trains.

STREAMLINING With the reorganisation completed, the second step toward meeting the challenges ahead was for each of the groups to undergo a massive streamlining and process improvement exercise within their areas of specialty. The order of the day was to automate wherever possible. Automation was no longer a "nice to have", but a "must have".

As a result, treasury transitioned into full electronic banking for all offshore payments. Increased pressure was placed on the local banks to meet Qatargas's electronic banking needs. Nevertheless, this was only the first step toward the ultimate goal of implementing a fully automated, straight-through processing payment system via SWIFT.

Administering the bank accounts as imposed by the lenders was a major challenge. Paying an invoice from a bank account other than that specified in the agreement was considered a violation. With the volume of payments envisaged across all ventures, it was almost impossible to monitor the correctness of all transactions, so treasury had to figure out a way to control this process automatically. Contrary to usual practice, treasury began to actively influence the accounting design to hard-wire lender account management restrictions into the venture set-up of each company, thus enforcing compliance through the ERP system.

Qatargas made use of the well-established ERP system as a base for its treasury management system.

One of the most basic improvements in this area was a centralised view of cash balances across all companies for bank and book. This allowed cash management staff to assess the cash position and immediate funding requirements for each venture without having to access their individual bank statements and accounts payable modules.

Treasury funding transactions and vendor payments were completely automated. Manually typed bank letters became an outdated practice. These improvements saved time and minimised the human error associated with manual processes.

The system was also configured to allow for daily automated bank account reconciliation. Entries on the bank statements, made available by the banks in MT940 formats, were matched to open items in the ERP system based on the amount and unique reference number for each transaction. This allowed treasury operations staff to identify delayed payments, delayed receipts and ambiguous debits to any bank account early enough on the following banking day to enable timely investigation and resolution.

Investments were also managed to a great extent using the existing ERP system. Authorised investment counterparties and limits were managed centrally, preventing dealers from entering into transactions with counterparties that did not meet the permitted investment criteria of Qatargas or the lenders.

Investment placement from the offer stage to trade confirmation and settlement was now entirely automated. Offers for each deal were saved in the system to create an audit trail. Upon execution of the offer in the system by the dealer, a trade confirmation with all the relevant details for the deal was now generated automatically. The automated process was designed to segregate the duties and authorities between front-office, middle-office and back-office staff, increasing internal controls over this high-risk activity.

Bank account administration was also enhanced by streamlining the bank operating mandates across all companies. This allowed treasury to communicate changes in banking instructions and authorised signatories promptly and efficiently to all relationship banks.

Treasury management as a discipline is always forward-looking, making the anticipation of change the only constant. It was therefore, important to build a treasury system and organisation that could accommodate change with agility and ingenuity.

The changes at Qatargas did not happen overnight. It took the time and effort of many dedicated individuals who had to manage to keep the daily business running while creating and testing the processes and systems that will serve Qatargas for years to come.

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