Greensill

Greensill submission to the Senate Education and Employment Committee on the Payment times Reporting Bill and the Payment times Reporting (consequential ammendments) Bill

- **Greensill supports the Bills**
- **Consistent definition of a small business is essential to implementing a payment times reporting framework.**
- **A registry of small businesses or another mechanism would smooth implementation**
- **Supply chain finance needs to be defined and reporting should include other means by which businesses bring forward payment times.**
- **Any reporting regime should include appropriate protections for commercial-in-confidence information**

SUMMARY

Greensill welcomes the opportunity to provide a submission to the Senate Employment and Education Legislation Committee inquiry into the Payment Times Reporting Bill 2020, and the Payment Times Reporting (Consequential Amendments) Bill 2020.

As Senator Simon Birmingham noted in introducing this Bill on 12 June 2020,

> *"Longer payment times hurt small business cashflow and this harms their ability to hire, invest and grow. Cash-constrained small businesses are often forced to seek out expensive forms of financing in order to sustain their business operations. Late payments also have a flow-on effect across the economy as small businesses paid more slowly, pay their suppliers more slowly in turn."*

We support Senator Birmingham's statement given the important role small businesses play in the Australian economy as creators of wealth and employment. Greensill was established to help businesses accelerate their growth by bringing forward payments from their customers, in turn allowing them to avoid taking on expensive debt to pay their own bills. The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) found in her final report that supply chain finance (SCF) provide benefits to both small suppliers and large buyers and should be available to small businesses to help them reduce payment times from 30 days to better terms.

Greensill agrees with the purpose of the legislation to monitor the performance of large companies against their own payment terms. Late payments are a significant source of stress on any business.

Greensill also supports the proposed definition of a small business and the use of 30-day terms as a yardstick against which to measure payments by large companies to their small business suppliers. However, we note that there is difficulty in identifying or verifying which suppliers fit the description. We would be happy to help with this process.

We note that the legislation would require reporting entities to disclose their use of SCF in reporting on their payment terms and practices. However, there is no definition provided and it is not clear what information is to be provided. We would ask that the legislation include references to other methods used by business to manage payment times.

ABOUT GREENSILL

Greensill is a leading non-bank supplier of working capital finance to companies around the world. In Australia Greensill provides a range of working capital finance products, including supply chain finance, to companies across industries ranging from agriculture to telecommunications, mining and construction. In 2019 we financed $US143 billion ($208 billion) of payments to eight million customers and their suppliers in 175 countries. The company was founded in 2011 by Lex Greensill, who grew up on a Bundaberg sugar cane farm where it could take up to two years to be paid for a crop.

LATE PAYMENTS AND EXTENDED PAYMENT TERMS

This legislation has been prompted by concern about late payment practices and extended payment terms. Late payments can be a cause of significant stress in any business. However, it is important to distinguish between late payments, which are payments made later than the agreed payment terms, and payment terms, which may be agreed between a customer and their supplier and may include terms beyond 30 days. The two are often conflated in public discussion about payment practices. These bills should mark an important step in making that distinction.

Many businesses will have valid industrial, contractual, seasonal and commercial reasons for seeking extended payment terms from their suppliers or their customers. Examples of these could be seasonal industries, such as agriculture, progress or milestone payments on construction contracts and export manufacturing where payments from customers are delayed while goods are being shipped. Ensuring payments throughout these supply chains are consistent with the receipt of payments from end customers is essential to the financial health of the entire supply chain.

However, this does not negate the need for 30-day payment terms to small businesses within that supply chain and we are fully supportive of this as a default position.

DEFINITION OF SMALL BUSINESS

Greensill notes that the definition of small business is left to be described in the rules. Greensill supports a proposed consistent definition for small businesses as being turnover of up to $10 million per annum for the purposes of reporting payment terms. The definition is consistent with that used by the Australian Taxation Office.

We would advocate that the ASBFEO or the proposed Payment Times Reporting Regulator maintain a small business registration database that could be used to check the status of suppliers declaring as a small business.

We note there are conflicting descriptions of small and large businesses used by different regulators different legislation. For example, since July 2019, the Australian Securities and Investments Commission has determined that a business is 'large' and must provide financial reports if it meets two of the following criteria: turnover of $50 million or more; gross assets of $25 million or more; or 100 or more employees.

> *If the company does not meet at least two of the above criteria, it is 'small'.*[1]

The designation as 'small' means that in most cases they will not file financial reports that could be used to independently verify their status as a small business.

SUPPORT FOR 30-DAY TERMS FOR SMALL BUSINESS

In Section 14 (d), the proposed legislation requires reporting entities to:

State the proportion, determined by total number and total value, of small business invoices paid by the entity during the reporting period in accordance with each of the following:

- less than 21 days after the invoice was issued;
- between 21 and 30 days after the invoice was issued;
- between 31 and 60 days after the invoice was issued; and
- more than 60 days after the invoice was issued.

Although the proposed legislation does not specify that small business suppliers should be paid within 30 days, we note that much of the discussion about this legislation, including research cited on payment practices, uses 30-day terms for small business as a yardstick.

We believe this is a good benchmark and have publicly advocated for it. Companies should pay their small business suppliers within 30 days or less.

It would also be worthwhile to encourage electronic invoicing to streamline processing and help facilitate faster payment times for business.

[1] www.asic.gov.au/regulatory-resources/financial-reporting-and-audit/preparers-of-financial-reports/are-you-a-large-or-small-proprietary-company/

SUPPLY CHAIN FINANCE (SCF)

Greensill notes that Section 15 (3) of the proposed legislation requires reporting entities to provide information on their use of SCF in paying small and medium enterprises.

> *"Without limiting paragraph (1)(i), information or documents prescribed by the rules for the purposes of that paragraph may relate to the entity's payment terms or practices, including supply chain financing, during the reporting period in relation to small business payments."*

However, it does not provide a definition of SCF or the types of products and services that would be included or excluded from the reporting requirements or what information should be provided. We understand that it is intended to have definitions and other matters addressed in the rules and regulations to be administered by the relevant minister.

However, we are concerned that the absence of a definition, or an incorrect definition, in the legislation would not capture the full range of products that a supplier or customer would use to manage payment times.

Nor does the legislation require any detail on the impact that the use of SCF – or similar financial products – has on an individual company's payment times for suppliers.

The legislation could be amended to require disclosure of whether the large business facilitates, allows or otherwise takes advantage of any sort of early payment program or arrangements for or with their suppliers.

One definition of SCF – sometimes referred to as reverse factoring – was provided in a recent review by the International Financial Reporting Standards (IFRS):

> *"In a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers and the entity agrees to pay the financial institution at a date later than suppliers are paid."*[2]

Another was provided in a recent report from credit ratings agency Standard & Poor's.

> *"A supply chain finance program is commonly set up by a corporate buyer with a bank or alternative provider to allow suppliers to get paid early for an invoice, usually at a discount. This method, known also as payables finance or reverse factoring, is particularly valuable for SMEs, who can access more affordable funding because the cost is based on their buyer's credit rating."*[3]

SCF is only one of a number of ways that a company of any size might seek to manage its working capital and payment times. There are other methods that the legislation should consider including in the reporting requirements.

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[2] www.ifrs.org/projects/work-plan/supply-chain-financing-arrangements-reverse-factoring
[3] www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/supply-chain-finance-grows-amid-pandemic-but-faces-stark-risk-warnings-58841608

They include:

- Early payment discounts offered by a buyer to their supplier
- Traditional factoring, in which a company sells its customer receipts to a third party at a discount to face value in exchange for cash up front. The financier offers a discount and collects the sums from customers.
- Dynamic discounting, where a business auctions its invoices either to the customer or to a third party via a marketplace, for early payment in exchange for a discount. Rates are set by the buyer, who also drives utilisation.

Alternatively, a business might use a credit card, term debt secured against its assets or other forms of borrowing that are all materially more expensive than being paid by SCF.

Among the benefits of SCF for suppliers are:

- Using SCF, small suppliers can get paid early, providing them with working capital that allows them to compete with bigger suppliers who are able to manage longer payment terms;
- Payment is much faster than usual – typically 1-10 days from time of invoice;
- The cost of SCF is materially less than borrowing, even taking in to account extended terms, because it is based on the credit rating of the customer, which has the obligation to repay the third-party financier. Typically, it is provided at an average annualised interest rate of 1-7 per cent;
- Suppliers are able to avoid or reduce their reliance on more expensive forms of borrowing that may be used to bridge the difference between their own expenses such as weekly or fortnightly wage bills, raw material purchases and rent while they wait to be paid, even on 30-day terms;
- Access to SCF is voluntary and would only be used by a supplier if it was cheaper than their existing finance facility and/or enabled them to bring forward payments that could be used to reinvest or accelerate the growth of the business.

In Greensill's experience 20-80 per cent of suppliers take advantage of SCF if it is offered by their customer, suggesting that they see value in the service. Even on 30-day terms for small business we would expect that there will still be demand for the service.

In his second reading speech, Senator Birmingham noted research demonstrating that in 2017-18 payments from large to small business were worth about $281 billion, with $77 billion of these payments paid later than 30 days. Expressed another way, this would mean that companies need to find $77 billion to meet shorter payment terms.

This echoes Greensill's own estimate – provided to the ASBFEO – that large companies would need to find an additional $65 billion in working capital in order to meet mandatory 30-day payment terms for all business, large or small, as the ASBFEO had recommended in its interim report.

These figures highlight the value of flexible payment times to large companies. Enforcing mandatory payment times for all business would require them to borrow or raise additional capital and care should be taken not to dissuade or discourage the use of SCF as the impact to supply chains and larger businesses could be extensive.

DISCLOSURE OF SUPPLY CHAIN FINANCE

In the *Bills Digest* for the legislation it is suggested that the negatives around SCF include that it is not properly disclosed in the accounts of businesses and that it is used to hide or disguise borrowings by a company.

Greensill supports transparency and consistency regarding the reporting of the use of SCF arrangements, including in company balance sheets.

While disclosure of the use of SCF is not a material concern for providers of SCF, disclosure of the use of SCF should be designed to harmonise with international reporting requirements as any misalignment with international accounting standards is likely to cause ongoing compliance and reporting problems for companies. At present a number of public companies already voluntarily disclose their use of SCF to the Australian Securities Exchange.

It is worth noting that the Interpretations Committee of IFRS completed a review of reporting requirements for SCF, or reverse factoring, in June, which found that there was no need to establish new standards for reporting.

> *"The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine the presentation of liabilities that are part of reverse factoring arrangements, the presentation of the related cash flows, and the information to disclose in the notes about, for example, liquidity risks that arise in such arrangements. Consequently, the Committee [decided] not to add these matters to its standard-setting agenda."*[4]

The IFRS review was undertaken at the request of Moody's Investor Services to aid its understanding of how SCF might affect the credit ratings of companies. We note that ratings agencies have already moved to take SCF into account when determining ratings.

Earlier this year Standard & Poor's said:

> *"We may treat drawings under a reverse factoring facility as a debt-like obligation in cases where the customer or supplier generates a material working capital benefit."*[5]

Greensill founder Lex Greensill has stated publicly on a number of occasions his view that rating agencies should consider credit provided by suppliers to be a financial liability.

[4] www.ifrs.org/projects/work-plan/supply-chain-financing-arrangements-reverse-factoring
[5] Reverse Factoring Is A Sleeping Risk, Report Says – S&P Media Release, March 8

> *"A dollar of liability to a trade creditor is the same as a dollar of a liability to a financial institution.," he said.*[6]

We would ask that in setting reporting requirements for SCF every attempt is made to ensure they are in line with international reporting requirements so as not to create additional burdens on businesses who use the service.

PROTECTION FOR COMMERCIAL IN CONFIDENCE INFORMATION

Finally, we note that the bill provides limited protection for commercial in-confidence information.

Greensill asks that the disclosure regime does not require reporting entities to identify individual providers of SCF, the value of individual contracts or the terms under which the service is provided as this could be considered to be valuable information to competitors.

Any documents identifying the provider of SCF or the terms on which they do business should not be disclosed to the regulator or, if they are disclosed, should not be made public by the regulator.

CONCLUSION

Greensill supports the aims of the legislation to highlight the performance of large companies against their payment terms for small business suppliers. We look forward to the progress of these Bills.

[6] https://www.afr.com/companies/financial-services/reverse-factoring-unlocks-dollars-makes-sense-for-suppliers-20191119-p53bvr