

Response to Position Paper on Supply Chain Finance Review.

Introduction.

1. Danny Sargeant is a retired Chartered Accountant having started his career in a big 4 firm. He moved to industry in increasingly senior accounting roles both in Australia and overseas. He progressed to be CEO of the Australian subsidiary of a multinational IT company. In 2005 he purchased a 50% share of a small Australian based IT reseller.
2. My interest in supply chain financing (SCF) arose from a request from Telstra to accept 62 days from month end supplier payment terms (SPT) and the offer of access to SCF. Two transactions occurred while this regime was in place giving me firsthand exposure to SCF. We resisted the imposition of extended SPT by Telstra and eventually obtained their agreement to leave our SPT unchanged.
3. Following this my on-going concern was that Telstra's example of extending SPT would cascade through the Australian economy following the example of foreign multinationals who have a propensity for doing this.
4. Conclusions I have drawn based on my experience are:
 - The underlying problem is extended SPT, and
 - SCF of itself is not a problem but is when combined with extended SPT.
5. The Position Paper has largely reached the same conclusion with the first 3 draft recommendations addressing SPT.
6. This response to the Position paper is split into 2 parts dealing first with extended SPT and second with SCF. I will then address the questions for comment for completeness.

Extended Supplier Payment Terms.

7. Trade payables are the amounts owing to suppliers of goods and services where there is a delay between the delivery and invoicing of the goods and services and payment of the associated invoice. SPT should reflect a reasonable time to allow the approval and payment processes to settle the invoice. Historically in Australia this would have rarely exceeded 30 days from end of month. Often it was faster. More recently modern IT systems and electronic payments render 30 day from invoice payments entirely achievable.
8. The Federal government is setting an example with 20 day payment terms for the vast majority of its purchases and has indicated its preference that industry follows that example.
9. Draft recommendation 3, "30 day payment standard The minimum standard for all supplier payments (regardless of supplier size) should be 30 days" has my full support.
10. In my view for this to work there needs to be broad acceptance through the entire community. The Federal Government has set an example that can underpin this. It needs to do more to demonstrate its commitment. The proposed Payment Times Reporting Framework (PTRF), currently at draft legislation stage, should be implemented to encompass reporting of payment terms and actual payment times by all large businesses to all non-large suppliers, not just small suppliers. This would have the added benefit of removing issues of definition of small business for the purposes of this legislation. The Federal Government must also follow through on its 21 November 2018 announcement that it "will require those same large businesses seeking to tender for government contracts to match our 20 day policy". Things to consider with this are whether the demand should be for 30 day payments and if the PTRF reporting can be used in

assessing eligibility and compliance. The Federal Government also needs to highlight its view to foreign owners of Australian based businesses. One way to do this would be to include a requirement in FIRB approvals of foreign takeovers that the acquirer agrees to adopt SPT that are aligned to those accepted in Australia or currently followed in the industry.

11. These recommendations stop short of a legislated regime. There are several reasons for this. I believe most customers do strive to pay their bills according to agreed terms. Their actions, when they can't for one reason or another, should not be made illegal. Good customers will deal with their suppliers in an ethical way and strive to make things right. Transparency, through the PTRF, will highlight the recalcitrants.
12. Unfair SPT exist where there is an imbalance of power between a powerful customer and a weaker supplier. In my view the ACCC should be the regulator charged with responsibility for monitoring and enforcing acceptable SPT behaviour. Obviously appropriate legislation should support the ACCC in this role.
13. Australian Consumer Law (ACL) already includes some provisions that are relevant. One is the concept of unconscionable conduct. The Australian Competition and Consumer Commission (ACCC) states "Unconscionable conduct is generally understood to mean conduct which is so harsh that it goes against good conscience." Imposition of extended SPT, say more than 30 days from invoice, and repeated failure without reasonable cause to meet those SPT, by a stronger customer on a weaker supplier should be deemed prima facie unconscionable conduct. Another is unfair contract terms. This legislation could be revised to deem payment terms exceeding, say 30 days, unfair.
14. In addition to the Federal Government actions listed above other steps need to be put in place. Business needs to be brought on board. Industry bodies may be a good way to achieve this. I suggest it should include but not be limited to:
 - Business Council of Australia (also see below)
 - Australian Industry Group
 - Chartered Accountants Australia and New Zealand
 - CPA Australia
 - Australian Institute of Company Directors
 - ASBFEO
15. State Governments should also be encouraged to implement consistent legislation with that envisaged by the Federal Government requiring businesses seeking to tender for their contracts to match the States' payment terms, appropriately short.
16. Consideration should be given to the accounting treatment of Trade Payables in financial statements. Historically all amounts owing to suppliers have been classified as Trade Payables. This should continue to be the case where SPT are reasonable, say 30 days. However, where longer SPT are mutually agreed I believe the arrangement can be viewed as a financing agreement as opposed to a trade agreement. This is certainly the way suppliers view it. As such I believe the resulting liability should be classified by the purchaser as a finance liability. It would still be classified as a current liability. A result of this classification would be that the movement in the financing liability balance would appear as a financing cash flow rather than an operating cash flow. I believe this would more properly present a "true and fair view". It would also partially address the concerns being raised by analysts such as Moody's and S&P.

17. I believe the combination of these various approaches would build a business culture in Australia of reasonably short payment terms to the benefit of weaker suppliers and the national economy.

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18. SCF is a solution looking for a problem. Extended SPT provide the problem. If the problem of extended SPT is dealt with adequately the demand for and use of SCF will be minimal.

19. Draft recommendation 4 SCF as a real choice SCF should be available to ~~small~~-business to reduce payment times from 30 days to better is fully supported.

20. Where use of SCF is not imposed but available suppliers are in the best position to decide if the product available to them is appropriate compared to alternative finance available to them.

Questions for comment.

1. Consistent small business definition.

a. I believe the issues discussed above are relevant to suppliers smaller and/or weaker than their customers. Dealing with just “small” suppliers encourages customers to take advantage of the not small but weaker suppliers. This should be avoided. If there is to be a definition it should be “small suppliers”. For this definition I think it should follow the format being roughly followed by the Federal Government, Rio Tinto and Telstra.

b. It would include:

- Turnover with supplier, or
- Total Turnover of supplier, and
- Include most suppliers, say 80%.

2. Enforceable payment times.

a. I believe it would be preferable to have BCA participation in supporting a culture of short SPT. The Australian Supplier Payment Code could be the vehicle to do this, but it would need some revision. It should be mandatory for BCA members. The PTRF could provide the performance measurement. BCA should review performance and impose appropriate sanctions if appropriate.

b. The PTRF should provide information. Sanctions should apply to non-reporting or inaccurate reporting. Of itself it would not enforce payment terms or times. It would effectively name and shame.

3. 30 day payment term standard

- a. Paragraph 9 above.
b. Paragraph 10 above.

4. SCF as a real choice

- a. Paragraph 18 above.
b. Paragraph 19 above.

5. Appropriate coverage by accounting standards

a. The AASB should consider the accounting treatment of Trade Payables as discussed in paragraph 15. Any remaining issues with SCF could be dealt with via notes to the accounts as considered appropriate by the AASB.

b. I think both the AASB and auditors should be considering the substance of these financing transactions and treat them accordingly.

- c. If the big end of town deals with the issues appropriately there will be no significant issues for small and family business accountants.
6. Further questions from competition & regulated financial product perspectives
- a. This is a much bigger issue. I think a supplier should expect confidentiality of their information with a customer. In today's sharing world this may be a dream.
 - b. If SCF is relegated to an appropriate role I don't believe there is a need for the disclosure suggested. I do believe that there should be full and clear disclosure of the terms between the finance provider/platform provider and the supplier avoiding "tick the box" acceptance of terms and conditions.
 - c. Paragraph 12 above.
 - d. I think there is a reasonable argument that the finance provider/platform provider should be regulated in some form. I'm not sure what form that should take and whether its ASIC or APRA.
 - e. With minimal use I don't believe this is a problem.
 - f. Yes
 - g. I don't see a need to report the rate publicly.
 - h. See d. above.
 - i. As SCF is a financing product I think suppliers should be able to take complaints to the AFCA.