

27 February 2020

Ms Kate Carnell AO  
Australian Small Business and Family Enterprise Ombudsman  
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Level 2, 15 Moore Street  
CANBERRA ACT 2601

By email: [inquiries@asbfeo.gov.au](mailto:inquiries@asbfeo.gov.au)

Dear Ms Carnell

### Supply Chain Finance Review Position Paper

1. This submission in response to the Australian Small Business and Family Enterprise Ombudsman (**ASBFEO**) Supply Chain Finance Review Position Paper (**Paper**) is made by the SME Business Law Committee of the Business Law Section of the Law Council of Australia (**SME Committee**). The SME Committee focuses on small and medium-sized enterprise (**SME**) issues and has a keen interest in this matter.
2. The SME Committee welcomes the opportunity to provide comments on the draft recommendations set out in the Executive Summary of the Paper and to respond to the questions that relate to those recommendations as posed in the Paper.
3. The Committee supports any move by ASBFEO to standardise payment times to small business and to have supply chain finance (**SCF**) methods recognised as regulated financial products.

### Key Points

4. The Committee supports:
  - (a) having the methods of SCF recognised as regulated financial products; and
  - (b) the providers of SCF being regulated by the Australian Securities and Investments Commission (**ASIC**) as Australian Financial Services Licence (**ASFL**) holders.

### Submission

5. The SME Committee's response to each of the draft recommendations set out in the Executive Summary of the Paper, and the Committee's answers to the questions that relate to each of those recommendations are as follows:

Draft Recommendation 1: Consistent small business definition

*The small business definition adopted across Government should be either to (a) simply define small business as not including, say, the top 100 companies or (b) a small business has fewer than 100 employees, with satisfaction of either (a) or (b) being sufficient to qualify as a small business.*

6. The SME Committee would prefer a definition of 'small business' based on a choice of either employee numbers or annual turnover (preferably \$10 million) rather than referencing the definition to either non-ASX100 companies, which would effectively include many companies that under any other definition would not qualify as a small business, or only to employee numbers, which by itself is a definition that can prove difficult to apply in practice.

Questions regarding the consistent small business definition

*Question 1a. For consistency, should there be a single definition of small business for payment terms?*

7. The SME Committee is aware that there are currently a range of definitions used for small business, based on number of employees, some fewer than 20, others fewer than 100, or based on turnover, including up to \$10 million or, alternatively, a combination of employee numbers and turnover.
8. It is the SME Committee's position that it would be of great benefit for the definition of 'small business' to be standardised across all legislation that provides protections for small business from unacceptable activities of big businesses.

*Question 1b. If so, what should that definition be? (For example, \$10m turnover?)*

9. The SME Committee prefers a definition of small business that is based on a choice of either turnover, preferably \$10 million, or employee numbers, preferably up to 100.
10. It is the SME Committee's position that a definition of small business only based on employee numbers is not appropriate. Identifying the number of a supplier's employees is difficult to ascertain in practice, especially where employee numbers fluctuate seasonally. This is especially in the case of agricultural suppliers.
11. In such instances, defining small business based on employee numbers places both buyers and suppliers in a difficult position – within a financial year a supplier may fall within the definition at sometimes, but not others. This places an unnecessary burden on both parties who would need to continuously monitor employee numbers and make appropriate disclosures in order to ensure compliance.
12. The Committee notes that there is currently also a review being conducted by Treasury on Enhancements to the Unfair Contract Term protections contained in the *Competition and Consumer Act 2010* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**). The appropriateness of the definition of small business in the legislation for those protections is included in that review. If that review results in the definition of small business being amended, then the Committee would support such an amended definition provided it addressed the Committee's concerns raised herein, and the definitions are the same.

### Draft Recommendation 2: Enforceable payment times

*The Supplier Payment Code should be replaced by the Commonwealth Government's Payment Times Reporting Framework with that Framework being administered and enforced by an appropriately funded, empowered and proactive entity.*

13. The SME Committee Does not support the introduction of mandatory payment term requirements for small businesses. The Committee notes that voluntary codes in a range of industries do not result in changes to behaviours for all members of an industry. It is only when behaviours are made compulsory that those industry members who would otherwise not comply with the Code requirements, will do so (because they have to or will suffer a penalty).
14. However, the SME Committee considers in its current form, the Commonwealth Government's Payment Times Reporting Framework is insufficient to address small business SCF concerns as identified by ASBFEO.

### Questions regarding enforceable payment times

*Question 2a. Is there a need for a mandatory Supplier Payment Code?*

15. Yes, so long as it does not mandate payment times.

*Question 2b. What role does the proposed Commonwealth Government's Payment Times Reporting Framework have in:*

*i. Assessing payment terms performance when SCF is utilised; and*

16. It is the view of the SME Committee that the proposed Commonwealth Government's Payment Times Reporting Framework will not provide any assistance to small business suppliers or to government for monitoring purposes in assessing payment terms performance of buyers when SCF is utilised.
17. When SCF is used by a buyer to pay a small business supplier, the buyer will be able to report its payment times under the proposed framework as being the payment time in which the small business supplier actually receives payment under the SCF arrangement. However, the small business supplier will not have received full payment of the amount they invoiced to the buyer as they will have suffered a discount on the amount they accept as payment in order to have received payment in accordance with the payment times reported by the buyer under the proposed framework.
18. The proposed framework does not look behind the payment times that are actually made and reported, and it may not be possible to assess, when a buyer reports its payment times in accordance with the framework, whether the buyer uses SCF with the result that the small business supplier has suffered a discount on the amount they accept as payment of their invoice.

*ii. Auditing and issuing fines or other sanctions for non-compliance?*

19. The SME Committee notes that the proposed Commonwealth Government's Payment Times Reporting Framework will also not provide any assistance to small

business suppliers or to government for monitoring purposes when auditing or sanctions for non-compliance under the regime are undertaken or applied.

20. The proposed regime only requires regular reporting of payment times and any auditing of the data in those reports would not include any recognition of the use of SCF nor any other terms or conditions of the terms of trade between the buyer who must report and a small business supplier. Any sanctions imposed on a buyer would be for not reporting, not for any other behaviour, such as making late payments.

*Draft Recommendation 3: 30 day payment standard*

*The minimum standard for all supplier payments (regardless of supplier size) should be 30 days.*

21. The SME Committee does not support this recommendation.

Given the objective is to look after suppliers who are small business people, if payment times to suppliers are mandated, no matter for how many days and whether from date of invoice or from end of month, a small business supplier who has received a payment from a buyer who becomes insolvent would be unlikely to be able to defend a claim for a preference payment raised by the liquidator of the buyer. The Committee considers it is important for small business suppliers to retain the ability to be able defend a claim for repayment of a preference payment by being able to argue that a payment received was in accordance with industry practice, which may differ from the payment time in its terms of trade, and be outside the preference payment repayment period.

The Committee also notes that it is not uncommon in industry for 30 day terms to be interpreted as '30 days EOM (end of month)', so that accounts payable officers can sensibly manage the payment of invoices from a single supplier by consolidating them and paying upon monthly statement. To impose a strict payment term of 30 days from date of each invoice would place an unreasonable administrative burden on the buyer.

*Questions regarding the 30 day payment term standard*

*Question 3a. For consistency, should there be an economy wide 30 day payment term mandated?*

22. As set out above, the SME Committee does not support this recommendation.
23. The SME Committee recognises that there are many examples of legislation that impose implied contractual provisions. That said, given payment terms are a fundamental element negotiated in commercial contracts, the Committee also recognises that it would be most unlikely for such 30 day payment terms to be able to be mandated.
24. The Committee accordingly suggests as an option that legislation could be put in place to make a contractual provision allowing a payment term in excess of 30 days to be voidable as is done in the Unfair Contract Terms legislation, on the basis that the inclusion of such a term is unfair to small business and not reasonably necessary to protect the buyer's legitimate business interests.
25. Should ASBFEO seek to mandate such a payment regime, the SME Committee requests that consideration should be given to the potential financial harm that could

be caused to small business suppliers who may later be faced with a buyer in liquidation. If a small business supplier is not paid within the mandated 30 days, but then receives payment later, even if only a short time later, from a buyer that later still goes into liquidation, the liquidator would pursue the supplier for recovery of preference payments under section 588FF of the Corporations Act. A supplier in that circumstance may have greater difficulty in raising a defence as it may not be able to argue that it did not have grounds to suspect insolvency of the buyer.

*Question 3b. For government contracts, how could 30 day payment terms be made to flow down supply chains to small business suppliers?*

26. The SME Committee is of the view that when government enters into contracts with its suppliers and includes 30 day payment terms, in whatever form, those contracts should include an obligation on the supplier to government to include in turn, in its contracts with its small business suppliers, the same obligation to make payment to those small business on 30 day terms.
27. The Committee also notes that should such payment terms become mandatory, as discussed in 3a. above, the term would need to be included in those flow down supply chain contracts with small business.

*Draft Recommendation 4: SCF as a real choice*

*SCF should be available to small business to reduce payment times from 30 days to better.*

28. The SME Committee considers that this position is dependent on the willingness and ability of SCF providers to make payments to small business suppliers on terms of less than 30 days, and the acceptability of the discount cost to small business suppliers of that quicker payment time.

*Questions regarding SCF as a real choice*

*Question 4a. Should SCF be available to small business to reduce payment times from 30 days to better?*

29. Yes, it should, although this is a commercial decision of the SCF providers and the small business suppliers impacted.

*Question 4b. What forms of SCF are of the greatest benefit to small business?*

30. The SME Committee recognises the benefits of SCF for small businesses, and that the development of electronic invoicing platforms and with non-bank finance providers looking to the credit rating of the big business buyer to support its SCF facility, enables small business to benefit from such funding without having to provide security to the funding provider.

*Draft Recommendation 5: Appropriate coverage by accounting standards*

*The accounting standards need to provide greater clarity and properly cover SCF to ensure that accounts cannot be manipulated, particularly to mask cash flow issues and insolvency.*

31. The SME Committee agrees with this recommendation for the accounting standards to be clear with regard to the purpose of SCF in the financial statements of the buyer.

Questions regarding appropriate coverage by accounting standards

*Question 5a. Should the Australian Accounting Standards Board (AASB) be consulting with its international counterparts to provide clarity as to how to capture and treat SCF in financial reporting?*

32. Yes, it should so that the International Financial Reporting Standards (**IFRS**) clearly cover SCF.

*Question 5b. Should auditors be given formal guidance to ensure consistency in the financial reporting (by note or otherwise) of entities using any form of SCF?*

33. Yes, they should in order to ensure consistency of approach.

*Question 5c. How do small and family business accountants become educated as to what SCF is and what its implications are for reporting?*

34. For small businesses that require audited financial statements, the IFRS (or AASB) standards must be complied with. For small businesses with non-audited financials, their accountants should be able to learn about SCF from their industry body as part of their annual continuing professional development requirements.

Draft Recommendation 6: Further review from competition perspective

*The ACCC should review SCF provider activity from an Australian Competition Law viewpoint, including how data is applied through using artificial intelligence and algorithms.*

35. The SME Committee prefers the position that the provision of SCF would be better accepted as the provision of a financial product and SCF providers should be subject to licensing and regulation by ASIC. ASIC, rather than the Australian Competition and Consumer Commission (**ACCC**), would monitor the conduct and disclosure obligations imposed on holders of AFSLs by Chapter 7 of the *Corporations Act 2001* (Cth) (**Corporations Act**), as well as the unconscionable conduct and consumer protection provisions under the ASIC Act, and obligations with regard to data, as it does for other providers of financial products and services.
36. The SME Committee is aware that as the application of data through the use of artificial intelligence and algorithms continue to be developing areas of law and regulation, both ASIC and the ACCC may look at considering how best to deal with SCF provider activity in these areas.

Questions regarding further questions from competition & regulated financial product perspectives

*Question 6a. What protections are required for small business that have their business performance data captured and stored by big business that may be shared with third parties?*

37. The SME Committee is of the view that, at the very least, any business performance data captured and stored by big business with regard to their small business suppliers must be deidentified if shared with third parties.

*Question 6b. Should a small business receive a copy of the contract between the finance provider or platform provider and the other party to the supply chain transaction (buyer)?*

38. The SME Committee believes that in order to ensure transparency and fairness of dealings with small business as suppliers under SCF arrangements, to enable a small business to be able to determine the actual economic benefit in accepting a discount on payment if its invoices, a provision for disclosure similar to those included in the Personal Property Securities Register (**PPSR**) legislation could be put in place. Such a provision would require only certain relevant commercial terms between the buyer and the SCF provider to be made available to the small business.

*Question 6b (cont). With the goal of transparency, what data should be shared between the provider and the buyer?*

39. The SME Committee believes that the buyer will need to share with the SCF provider the data necessary to enable the SCF provider to make early payment to the small business supplier. This will include details of agreed terms of trade between the buyer and the supplier, the amount of the supplier's invoice, the date of issue by the supplier and the date of approval by the buyer of the invoice, the discount to be applied for the actual payment to the supplier, and details of where to make the payment to the supplier.

*Question 6c. Is there a role that the ACCC needs to play in regards to unconscionable conduct or third line forcing?*

40. The Committee is of the view that there could be a role for the ACCC should the behaviour of a buyer in leaving a small business supplier with no option other than to enter a SCF arrangement in order to have its invoices to the buyer paid within acceptable time frames be considered to *prima facie* appear to be either unconscionable conduct or third line forcing.

*Question 6c (cont.). Are there any other areas that the ACCC should consider?*

41. The SME Committee notes that should the provision of SCF in future be dealt with as a financial product that requires its provider to hold an AFSL, ASIC would be the regulator and all the obligations of a licence holder under Part 7 of the Corporations Act would apply to that provider, including those that require fair and honest behaviour.

*Question 6d. Should a contract providing SCF in any form be regulated as to how it is implemented/utilised by a big business?*

42. The SME Committee considers that ASIC should revisit any application of ASIC Instrument 2017/794 which preserved the exemption to requiring an AFSL, and to the consequent hawking and disclosure obligations, that would otherwise have applied, and which was originally given by ASIC Class Order 04/239 to the practice of the factoring of debts that fell within the definition of a financial product by being considered a derivative.

43. The SME Committee considers that, in effect, SCF is a form of debt factoring, and the concerns for small business suppliers as identified by ASBFEO could be monitored and prevented if ASIC was to regulate SCF providers as holders of AFSLs.

*Question 6e. What mechanisms could protect small business users of SCF from the costs and administrative burden of having to engage with several buyer-led SCF providers?*

44. The SME Committee suggests that it could be useful for a website accessible to small business suppliers to be available to show comparison information of SCF product options and providers.

*Question 6f. Should the SCF provider report the effective annualised rate of interest charge/discount?*

45. The SME Committee is of the view that the SCF provider should advise the small business supplier of the effective annualised interest rate to enable the small business supplier to compare the SCF product being offered to other forms of SCF that may be available to it.

*Question 6g. Should the effective annualised interest rate/discount be reported publicly as a “comparative rate”?*

46. The Committee believes there would be no harm in the effective annualised interest rates/discounts being reported publicly as a ‘comparison rate’, perhaps on the website suggested in the Committee’s answer to Question 6e. above.

*Recommendation 7. Further review from regulated financial product perspective*

*Treasury and ASIC should review whether SCF should be a regulated financial product with coverage of rate setting.*

47. The SME Committee supports having SCF providers regulated. The provision of SCF in whatever form *prima facie* falls within the definition of a financial product. In essence its outcome is the same as factoring. Since 2004, ASIC has provided exemption for providers of factoring that would comprise a derivative under the definitions of financial products from having to hold an AFSL, on the basis of complying with conditions including having an internal dispute resolution service. In 2017, this exemption was extended and preserved through ASIC Legislative Instrument 2017/794. The Committee does not believe that rate (discount) setting should be regulated. Regulation by way of requiring SCF providers to hold an AFSL authorising the provision of SCF would allow ASIC to ensure that the conduct, conflict management, disclosure, dispute resolution and other obligations that apply to all AFSL holders are complied with by SCF providers.

*Questions regarding further review from regulated financial product perspective*

*Question 6h. Is there a role that the Australian Securities and Investments Commission (ASIC) needs to play?*

48. The SME Committee considers that ASIC should revisit any application of ASIC Instrument 2017/794 which preserved the exemption to requiring an AFSL, and to the consequent hawking and disclosure obligations, that would otherwise have applied, and given by ASIC Class Order 04/239 to the practice of the factoring of debts. In

effect SCF is debt factoring, and the concerns identified by ASBFEO could be monitored and prevented if ASIC was to regulate SCF providers as holders of AFSLs.

49. Given the concerns identified by ASBFEO with regard to *prima facie* unfair behaviour of big businesses toward some small business suppliers through the use of SCF, the SME Committee is of the view that ASIC could effectively prevent these unfair practices should providers of SCF be required to hold an AFSL.

*Question 6i. Is there a role that the Australian Financial Complaints Authority (AFCA) needs to play?*

50. Given that the nature of SCF is effectively a financial product akin to factoring, the SME Committee considers it would be appropriate to have any complaints about the provision of SCF, once dealt with by the provider's internal dispute resolution process, to be able to be referred to AFCA.

**Conclusion and further contact**

51. The SME Committee would be pleased to discuss any aspect of this submission.
52. Please contact the chair of the SME Committee, Coralie Kenny on 0408919082 or at [coralie.kenny@gmail.com](mailto:coralie.kenny@gmail.com), if you would like to do so.

Yours faithfully



**Greg Rodgers**  
**Chair, Business Law Section**