Slow payers face long-awaited scrutiny

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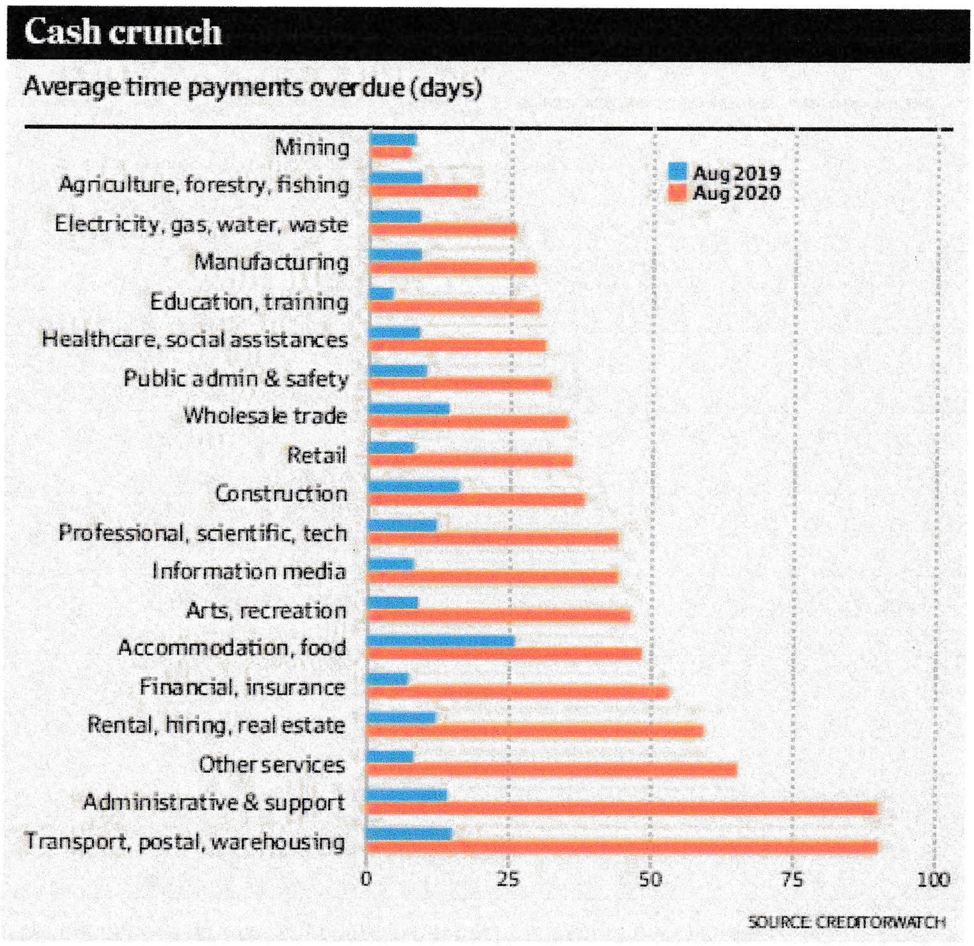
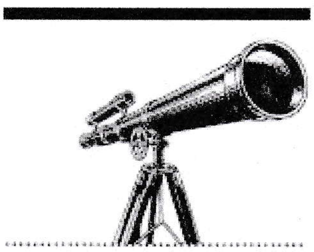


The cash crunch suffered by so many companies during the pandemic has not been equally shared around.

On Friday, retail group Premier Investments was one of the winners – delivering a better-than-expected 29 per cent jump in annual net profit to a record $138 million despite the travails of COVID-19.



Premier's strong cash balance – around $449 million at the end of its financial year, more than double the previous year – came at the expense of its suppliers.

Manufacturers had to wait much longer than usual – up to six months – for the money they were owed for delivering clothes and other goods to stores including Just Jeans, Peter Alexander and Smiggle.

Premier's financial accounts reveal that its trade payables, which reflect how much money it owes suppliers and other creditors, soared to $209 million from $81.9 million a year earlier, including $54 million to pay interim dividends.

Premierdeclinedtocommenton exactlyhowlongit tooktopaybillsbut saidtheJust

Group(whichownsthe clothingstorebrands)had"sought supportfromsuppliersfortemporary flexibilityinpayment terms"duringthe pandemicandwas nowprogressingto "moreusual"payment termsasthe viruseasesand somestoresreopened.

But at 120 days, even Premier's usual payment terms are far too long, well beyond the Business Council of Australia's recommended time frame of 30 days.

Big companies have been able to easily dictate payment terms because their small suppliers will typically miss out on sales altogether if they do not accept them. There have been no laws in Australia forcing companies to pay bills quickly (although federal and most state governments have prompt payment policies for their invoices) and companies have been under no obligation to disclose how long it takes them to hand over cash to suppliers.

But that will change from January 2021, when companies that earn more than $100 million a year will be required by law to reveal exactly how long it takes them to pay small suppliers, including the shortest and longest payment periods.

Federal Small Business Ombudsman Kate Carnell says some companies previously made excuses for delaying bill payments by defining small businesses as companies with less than 20 people or providing services worth less than $1 million a year.

ButinSeptember, theSenatepassed legislationapprovingtheintroduction ofthenew PaymentTimesReporting Schemewhichrelies ontaxlawto defineasmallbusiness –entitieswithan annualturnoverof lessthan$10million.

Big companies and government enterprises will be required to report twice a year on their payment terms and practices for their small business suppliers and the reports will be made available for all, free, on the internet.

The scheme is not as tough as the federal Small Business Ombudsman would like, because there are no financial penalties for companies that do not pay small businesses within 30 days. The only penalty is being named and shamed. There are fines for companies that do not report at all.

But Ms Carnell's office will closely monitor compliance (which is expected to cost companies about $22.5 million a year) and will push for tougher legislation if payments do not start speeding up.

Big companies will also need to disclose whether they use supply chain finance schemes, which require suppliers to accept a discount on invoices to get paid early.

Use of supply chain financing has risen during COVID-19, with Coalition, a research group owned by S&P Global, reporting that the schemes "continued to see robust growth due to rising volumes" in the first half of 2020 (it did not specify the exact volumes).

Greensill Capital, one of the biggest global providers of the schemes, claims only a few companies abuse them to pay suppliers late and that there will still be demand for the schemes after the new payment laws come into effect.

Thisyearit toldclientsinAustralia, includingconstructiongroupCIMIC, thattheycould nolongeraccessits financingtodelay billpaymentsbeyond 30daysafter theendofOctober, winningpraisefrom MsCarnellfor takinga"proactiveapproach".

But CIMIC, which now takes at least 60 days to pay suppliers, could simply find another supply chain financier if it does not want to pay all its bills within a month.

To fend off criticism of supply chain finance schemes, which have been used by several big companies that have collapsed due to accounting scandals including Abu Dhabiheadquartered NMC Health, Singapore's Agritrade and the UK's BrightHouse, financial providers have been on a PR offensive.

The global supply chain finance forum, which includes banks and other financial institutions, said in August that small businesses should never be bullied by companies into joining the schemes and transparency in reporting the use of the schemes was "desirable".

The forum also said the incidences of suppliers being forced into accepting unfavourable terms were "isolated and uncommon" and argued that the liabilities arising from companies' use of the schemes did "not create additional financial risk above and beyond those that already exist in trade between a buyer and a seller".

S&P Global Ratings analyst Graeme Ferguson agreed that there was nothing "inherently wrong" with supply chain finance, pointing out that it can increase a company's access to funding sources and improve the efficiency of its capital structure.

But Mr Ferguson said existing accounting standards still make it possible for companies to hide their use of supply chain finance facilities and that this can "obscure a company's underlying financial health and make a company appear to be more creditworthy than it actually is".

Regulators are pressing for more disclosure. In June, the US Securities and Exchange Commission sent letters to Coca-Cola and Boeing asking for more information on their use of supply chain finance.

TheregulatornotedCoca-Cola's accountspayablehadincreasedby around$1.1billion in2019afterdelaying paymentstosuppliersand thatituseda supplychainfinance program.Itwas askedtoexplain theimpactthe arrangementshadonoperatingcash flowandwhether itplannedtofurther extendpaymentterms.

It also asked the soft drinks group to consider disclosing changes in its accounts payable *days to provide investors with "a metric" of how supply chain finance arrangements impacted its working capital.*

Similar questions were asked of Boeing, whose financial statements showed $4.5 billion was payable to suppliers participating in supply chain finance programs.

Neither Coca-Cola nor Boeing have disclosed their replies to the SEC.

Meanwhile, lawsuits are cropping up against companies that have used the schemes. In August, CIMIC was hit with a suit filed in the Victorian branch of the Federal Court by class action firm Phi Finney McDonald.

The suit alleges that between February 2018 and July 2019 CIMIC's reported earnings were not derived from cash generation from operating activities, and were instead generated from "the receipt of factoring".

CIMIC uses both traditional factoring, which involves selling its invoices to financiers so it can collect cash early, and "reverse factoring" which is another term for supply chain finance.

The suit claims CIMIC's use of factoring meant its cash generation was not sustainable and that the company did not provide "a true and fair view of its financial position as at the reporting date to which the relevant financial report related" and that it consequently misled investors.

CIMIC did not reveal to investors until mid-2019 that it had entered into factoring arrangements with banks and financial institutions to sell its receivables, disclosing that its receivables factoring significantly increased to $1.99 billion at the end of June from $600 million in 2017.

The factoring was worse than analysts had expected, with Hong Kong's GMT research previously estimating that CIMIC had factored $1.2 billion of receivables.

CIMIC has subsequently disclosed more information, breaking out its use of factoring and reverse factoring. In its most recent update, at its half-year results in July, it said the level of supply chain finance across the group was $360.6 million at the end of June, down from $851.3 million at the end of December.

NMC Health, which is listed on the London Stock Exchange and was a user of Greensill's services, has also been hit with several class-action lawsuits after going into administration in April.

US short seller and research group Muddy Waters said in late 2019 that it believed NMC Health was inflating asset values and understating debt, materially misleading investors *"such as by trying to give investors the (false) impression it does not engage in reverse factoring".*