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Mr Sean Macintyre
Director, Small Business Policy
Department of Jobs and Small Business
By email: PaymentTimes@jobs.gov.au

Dear Mr Macintyre

PAYMENT TIMES REPORTING FRAMEWORK – DISCUSSION PAPER

The Office of the NSW Small Business Commissioner ('the OSBC') is focused on supporting and improving the operating environment for small businesses throughout NSW. The OSBC advocates on behalf of small businesses, provides mediation and dispute resolution services, speaks up for small business across all levels of government, and makes it easier to do business through policy harmonisation and reform.

We are strongly supportive of measures to deliver improved practices in relation to payment times. For small business, late payment is an issue of particular significance – most particularly when supplying to larger businesses.¹ Due to their power imbalance in dealings with larger businesses,² small businesses are unable to prescribe favourable payment terms. For the same reason, they are unlikely to pursue a remedy for breach of payment terms imposed by a larger customer.³ Many small businesses have insufficient time and resources to pursue more favourable arrangements in any case.⁴

Generally, late payment does not occur for legitimate or unavoidable commercial reasons.⁵ Rather, large business use small businesses as involuntary creditors, by delaying payment.⁶ Plainly, small businesses should not be made to play the role of a bank for their larger customers. But the practice is widespread - with almost \$50 billion paid late to Australian small and medium enterprises each year.⁷ Furthermore, around 40 per cent of small businesses frequently do businesses with operators whose standard terms allow them to make payment one month or more after the relevant sale.⁸

For the businesses bearing the brunt of late payment, this state of affairs reflects much more than large-scale inconvenience. There is an increasing recognition of the myriad of economic and social issues arriving from these practices. As each payment is proportionally more significant to a smaller operation,⁹ late payment has a particularly damaging effect on small businesses' cash flow.¹⁰ For many affected operators, this gives rise to a risk of insolvency¹¹ and even bankruptcy.¹² But even when the threat is less than existential, late payment can compel small business to downgrade employee and capital investment,¹³ redirect existing resources,¹⁴ and obtain bridging finance.¹⁵ A majority of small business owners also report that late payment has had an adverse impact on their physical and mental health.¹⁶

Nor is the impact confined to businesses awaiting payment. In particular, late payment forces small businesses to pay their own suppliers after time.¹⁷ But the final macroeconomic impact can restrain entire industries, sectors¹⁸ and even economies.¹⁹

For these reasons, the OSBC has already taken action to deliver faster payment terms for small business. We are driving implementation of the NSW Government's *Faster Payment Terms* - reducing our own payment times to 20 calendar days at present, and 5 business days by 2019. We are also advocating to Local Government NSW to endorse and implement faster payments in their dealings with small businesses. This extends the reach of faster small business payments to the billions of dollars our state's 128 Councils spend on procurement every year.

But we recognise that this issue cannot be resolved within the sphere of public procurement alone. We therefore welcome the Department of Jobs and Small Business' ('the Department') proposed payment times reporting framework for large businesses. By delivering increased transparency to payment practices, the initiative should incentivise improved behaviour by businesses required to report ('reporting businesses'), as well as deliver vital market intelligence to small businesses and other stakeholders.²⁰

We acknowledge that it is important that the scheme does not impart such a burden on reporting businesses as to discourage large businesses from working with small suppliers. But it is our view that a robust scheme can best achieve the benefits identified, without imposing an unreasonable obligation on those providing the data. Indeed, the collation of data likely to be required under the framework should not represent a disproportionate or unreasonable cost or time burden for reporting businesses. It is credibly suggested that businesses sufficiently large as to be captured under the framework are already collecting data on payment terms for internal purposes.²¹

In light of our own experience working to drive faster payments, and our engagements with businesses and experts to the same end, we offer the following commentary and recommendations regarding the specific questions posed in the discussion paper.

1. *What is the preferred scope of reporting; in particular, should reporting be limited to payment practices for small business? If so, how should small business be defined?*

Scope of reporting

Given that late payment practices are closely connected to the power imbalance between small suppliers and their larger customers, it is appropriate that the framework is designed primarily for the benefit small business. But in our submission, it does not follow that the scope of reporting should be limited to small suppliers alone. Rather, we suggest that reporting businesses should be required to provide data concerning their payment practices in relation to all suppliers.

The discussion paper contends that such a broad scope of reporting would prevent users from deriving precise insights into payment practices affecting small businesses specifically.²² However, provided that information provided through the framework allowed users to differentiate between payments to small businesses, and those made to other payments, no such limitation should apply.

In fact, a requirement to report on all payments should provide richer data to small business, as it would support a comparison between payment practices affecting small suppliers and other businesses.

<p>Recommendation 1: The framework should require businesses to report on payments to all suppliers.</p>

Definitional issue

Plainly, any framework allowing for comparison between payments to small business and other entities must prescribe a definition of 'small business', so to allow reporting businesses to collate data as required. Given the many definitions of 'small business' used by governments and others, we acknowledge that this issue is not without complexity.

However, the Australian Taxation Office already collects information concerning businesses' annual turnover, as businesses must declare total sales when lodging a Business Activity Statement.²³ If the framework were to utilise a turnover-based definition of 'small business', the information provided by reporting entities could be cross-referenced against existing ATO data on business turnover. This would allow for highly efficient, or even automated, identification of small suppliers. It would also require no additional information from either suppliers or reporting businesses.

Furthermore, our engagements suggest that the ATO's definition of a 'small business' – that is, one whose aggregated annual turnover does not exceed \$10 million²⁴ – is more widely used and understood than most competing definitions. The OSBC therefore suggests that the framework could employ this definition, to assist in delivering a streamlined scheme, as well as one that is well-understood by stakeholders.

We accept that current regulation may prevent the Commonwealth from using or providing data extracted from Business Activity Statements in the manner we advocate. If this proves an insurmountable obstacle, the use of an alternate definition may impart a considerable obligation on reporting businesses.

The popular Australian Bureau of Statistics definition of a small business²⁵ would require additional provision of information by suppliers, and may prove nebulous in the case of businesses that employ more or less than that number across any specified period. Small businesses may also wish not to provide any such information to their customers. Likewise, using the value of contracts or invoices provided as a proxy for the status of a supplier as a small business invites dysfunction. There is no necessary correlation between any one purchase any the size of the relevant supplier.

The OSBC therefore suggests that, if use of ATO data as described is impracticable, suppliers should simply be required to declare to reporting businesses whether they self-identify as a small business. The business could also be asked to disclose which definition of 'small business' that it believes it satisfies – for example, the popular Australian Bureau of Statistics definition providing that a small business is one employing fewer than 20 persons.²⁶

Recommendation 2: The framework should define a small business as one with aggregated turnover of \$10 million or less in the preceding year, and utilise existing ATO turnover data to identify suppliers that meet this definition.

Recommendation 3: In the alternative to recommendation 2, the framework should require suppliers to declare to reporting businesses whether they self-identify as a small business.

2. Who should be obligated to report under the framework? What reporting approach for related entities is going to be most useful for small business?

Entity and group reporting

In relation to reporting obligations affecting subsidiaries, the OSBC proposes that the requirement to report generally apply at the entity rather than group level. This will assist users to draw a nexus between behaviours and trends revealed by the data, and the actors most directly responsible. By contrast, consolidated reporting may assist to conceal the identity of those engaged in poor payment practises, or even obscure the behaviour itself.

However, we also concur strongly with the discussion paper's suggestion that an entity related to a larger business group should not be able avoid the obligation to report purely by virtue of its corporate structure.²⁷ We therefore suggest that an exception should apply to the general requirement to report at the entity level. That is, a business which is a subsidiary of one whose annual turnover is sufficient to meet the requirement to report, or which is a joint venture of multiple businesses required to report, should itself be required to report. This should apply even when the business' own turnover does not pass the relevant turnover threshold.

Recommendation 4: The framework's obligation to report should generally apply at the entity level. However, a business which is a subsidiary of a reporting business, or a joint venture of multiple reporting businesses, should itself be required to report - even when it would not otherwise be required to do so.

As regards the structure utilised by businesses required to report, the OSBC sees no reason why unincorporated entities should be afforded an exemption for reason of their unincorporated status alone. The small businesses that are to be the principal beneficiaries of the framework are equally affected by late payments, irrespective of whether a customer employs a corporate structure or some alternative. Allowing such an exclusion would thus constitute a considerable limitation and inequity in the reporting regime. It would also notably undermine the utility of the data collected.

The potential concern that unincorporated entities may be unaware of the obligation to report²⁸ could be addressed by way of an information campaign on the part of the Commonwealth – potentially in partnership with business representatives.

Recommendation 5: The framework should require both incorporated and unincorporated businesses to report.

3. *What payment information should be reported under the framework? What information is going to be most useful for small business (e.g. standard terms, payment times)?*

Information reported

In the OSBC's submission, there would be a measure of utility in the publication of data that meets all four categories of information that, per the discussion paper, could be provided under the framework.²⁹ Ultimately, however, faster payment must necessarily be measured according to the payment terms imposed by paying businesses, and their performance against those terms. Therefore, the success of the scheme in discouraging poor practice and providing market intelligence will ultimately depend on the provision of payment term and performance information. This data must therefore be required of reporting businesses, as a matter of priority.

The OSBC does not support the discussion paper's suggestion that businesses could be exempted from reporting on invoices valued below a prescribed amount.³⁰ This limitation would notably undermine both the utility and breadth of the data provided. As regards NSW Government procurement, 91% of purchases supplied by small businesses are relatively low value purchases of under \$10,000.

This information led us to implementing a two tier solution to small business payments, namely paying low value purchases under \$10,000 by government purchase card and faster payment terms for invoices up to \$1 million. We have further established that payment of every invoice is important to small businesses - given their limited resources³¹ and the importance of steady cash flow.³² Any such threshold would also complicate the reporting process.

Recommendation 6: As a matter of priority, the framework should require reporting of payment term data, and payment performance data.

Recommendation 7: The framework should not include a minimum value for invoices that businesses are required to report on.

Benchmarking

A large business that regularly meets the payment terms it imposes on small suppliers may not always provide genuinely fast payment. As noted above, approximately four in ten small businesses regularly trade with operators whose standard terms permit them to make payment more than one month after a sale. More concerning still, a small minority of businesses frequently do business with

purchasers whose standard terms allow for payment more than three months after supply.³³

To address this issue, reporting businesses should also be required to provide information around payments made against prescribed benchmarks. The United Kingdom's payment times reporting framework requires that businesses disclose the proportion of total payments made within increments of 30 days over the relevant period.³⁴ The Council of Australian Governments has agreed to pay invoices under \$1 million within 20 calendar days.³⁵ We therefore suggest an equivalent reporting requirement, aligned with this timeframe. Businesses would disclose the proportion of invoices paid instantly, within 10 days, within 20 days, and so on. Alternatively, the Commonwealth agency charged with publication of data under the framework (see our response to question 5) could prepare such figures, on the basis of raw data provided by reporting businesses.

Benchmarked payment data would provide very useful and easily comprehensive information. It would represent no more than a minor imposition on reporting businesses, irrespective of whether it is prepared by the reporting business directly or by a Commonwealth agency. It should therefore be adopted in the reporting framework.

Recommendation 8: The framework should require a reporting business to disclose the proportion of payments it made within instantly, and within increasing increments of 10 days, over the relevant period.

Definitional issue

To avoid confusion on the part of both users and reporting businesses, as well as inconsistency in the data, it is imperative that the framework prescribe a standard definition of 'payment term' (that is, 'days to pay').

For the majority of suppliers, the wait for payment is calculated from the day an invoice is provided to the relevant customer, to the day payment is made.³⁶ This is, we suggest, entirely reasonable. Supplying businesses are highly unlikely to be privy to any internal bureaucracy on the part of a customer, which may affect the payment time. Nor is it proper that a supplier's expectations should be adjusted in light of processes employed at the discretion of the customer, over which it has no control.

For much the same reason, the OSBC refutes the suggestion that any invoices lost by a reporting business should not be reported. From the perspective of a business awaiting payment, a lost invoice is simply a different form of administrative shortcoming delaying payment, for which the supplier is not responsible.

To this end, we note that both the NSW and Commonwealth Governments' *Faster Payment Terms* policies measure payment terms from the date the customer receives a correctly rendered invoice.³⁷

A requirement that the supplier provide a 'correctly rendered' invoice would also assist to manage the issue, raised in the discussion paper,³⁸ regarding the treatment of a disputed or incorrect invoice. Essentially, an invoice is rendered correctly if it

reconciles against the product provided, and includes all information necessary to process payment.³⁹ Thus, an invoice that meets these requirements is inherently correct, and should not give rise to any legitimate dispute.

Recommendation 9: The framework should provide that reporting businesses measures payment terms from the date a supplier provides a correctly rendered invoice, to the date it makes payment.

4. How should information be reported? In what situations will small business access the information?

Publishing model and format

To ensure that data collected under the scheme is searchable, accessible, comparable, and trusted by users, the OSBC submits that a centralised reporting mechanism, controlled by the Commonwealth, is nothing short of essential. Decentralised reporting would entail notable impracticality from a user perspective. It would also imply that the information was not prepared according to independently designed and prescribed requirements.

However, a central source of payment time information will not guarantee genuinely useful data in and of itself. In our view, the publishing model should support the needs of both small businesses seeking to access reporting information directly, as well as other stakeholders.

This should entail a dual approach. As most small businesses are too time poor to engage with late payment issues as a priority,⁴⁰ they are likely to prefer simple reports highlighting key facts. This should include payment term data and payment performance data, as well as businesses' performance against payment time benchmarks. There may also be merit in adopting a 'traffic light' system for such high-level reporting, as advocated by the British Small Business Commissioner.⁴¹ This would highlight a reporting businesses' overall performance in an immediately comprehensible manner, without explicitly criticising a business in a manner inconsistent with the role of the database as a non-partisan source of information.

We note further that the United Kingdom's payment times reports are published on GOV.UK⁴² – the central repository of British Government information and services.⁴³ Publication on a website that is already widely known and commonly used should assist in providing information in a manner convenient to small business. We suggest the Commonwealth's myGov website, or the ATO website, may serve as an equally suitable home for data published under the framework.

To further advance the status of the register as genuinely accessible, it must also be searchable according to multiple criteria applied to reporting businesses. That is, a small business should be able to search the register using not only a particular business name, but also industry, place of business, and similar.

In turn, regulators, advocates, researchers, and media representatives are likely to seek richer data. The activities of these parties are, of course, important in their own right. But advocates and the media, particularly, are also likely to act as intermediaries, providing information contained in reports to the small businesses affected. The central reporting mechanism should provide more detailed reports and data cubes, to adequately support the needs of these stakeholders.

Recommendation 10: Information reported under the framework should be published via an accessible, centralised resource.

Recommendation 11: The centralised reporting resource should provide both key, high-level data, as well as detailed reporting and data cubes.

Reporting frequency

So as to ensure that the framework provides information that is as relevant and up to date as possible, it is the OSBC's preference that reporting businesses captured under the framework are required to report quarterly. In addition, this would align reporting requirements with businesses' existing obligations to lodge Business Activity Statements quarterly; The NSW Government's own *Faster Payment Terms* requires also agencies to publicly report their performance on this basis.⁴⁴

To the same end, businesses should be required to provide reports no later than the quarter following that to which the report itself pertains.

At the very least, the scheme should require businesses to report twice yearly. For small operators seeking to make important commercial decisions, annual reports would not provide the requisite assurance that businesses were acting on timely and relevant information.

Recommendation 12: The framework should require businesses to report quarterly. It should further require that reports be provided no later than the quarter following the quarter to which they pertain.

5. How should the framework be administered? What is the preferred balance between regulatory certainty (through legislation and administrator powers) and flexibility (through standards and self-regulation)?

Preferred instrument

It is imperative that the framework be administered in such a manner as to provide that compliance is mandatory for all businesses captured under its reporting threshold.

The OSBC strongly supports the discussion paper's contention that a framework relying on any non-binding instrument would result in standardisation issues.⁴⁵

In our view, any voluntary scheme would also have a number of additional shortcomings. The United Kingdom experienced major issues with voluntary codes established to support reporting of payment times. These problems went to both consistent non-compliance by signatory businesses, as well as the limited proportion of businesses that agreed to report at all. As a result, both codes are now seen as ineffective and lacking in credibility⁴⁶ - and the British Government has implemented a mandatory code.⁴⁷

We suggest further that voluntary instruments may be inherently poor solutions to issues relating to a serious and systemic power imbalance between commercial actors. The franchising sector has been plagued with issues arising from the power imbalance between franchisors and franchisees.⁴⁸ The Australian Government established a voluntary franchising code in 1993 - and then moved to a mandatory

code just five years later, following a damning inquiry concluding that the scheme could not address abuse of power in the sector.⁴⁹ Likewise, in the food and grocery industry, major supermarkets hold much greater bargaining power than their small suppliers. Voluntary codes regulating that industry have been revealed to have major shortcomings in both the United Kingdom and Australia.⁵⁰

The Code should therefore be administered through a combination of legislation and subordinate regulation. So as to ensure an effective balance between certainty and flexibility, provisions establishing the reporting framework, and prescribing key obligations upon reporting businesses should be contained in legislation. Subordinate regulation should deal only with secondary or incidental issues.

Recommendation 13: The framework should be established by legislation, with secondary and incidental provisions prescribed in subordinate regulation.

Compliance and enforcement powers

Plainly, the Commonwealth agency tasked with administration of the framework must be afforded powers to investigate compliance issues among reporting businesses.

The agency must also be empowered to compel non-compliant businesses to report. These powers should extend to the capacity to both publish the names of non-compliance operators, and impose realistic and meaningful penalties for failure to comply. Without such powers, the force of Governmental mandate and oversight underpinning the scheme would be severely diminished. This would likely give rise to the same issues around compliance, and ultimately credibility, as would apply to any voluntary regime.

Indeed, the British Government's mandatory payment times reporting scheme does not include enforcement powers.⁵¹ It is suggested that this shortcoming at least partly explains issues of non-compliance that have arisen around that instrument.⁵²

Recommendation 14: The framework should empower the Commonwealth to investigate compliance issues; and to publish the names of, and impose financial penalties on, non-compliant businesses.

6. Should government agencies be subject to the framework and or comparable obligations?

Consolidation of data concerning payment times and practices can only assist the scheme to realise the prospective benefits of incentivising improved practice, and providing market intelligence. In this respect, any unnecessary separation of information related to the practices of private business, and those of Government, would represent a less than optimal solution. The OSBC therefore supports the option, proposed in the discussion paper,⁵³ that the Commonwealth transition from publishing its own payment times data in the *Payment times and practices* reports, to reporting under the framework.

Recommendation 15: Commonwealth Government agencies should be required to provide reports under the framework, rather than in separate reports.

Next steps

As improved payment practices are a matter of acute importance to small businesses throughout New South Wales, this issue represents a major and ongoing priority for the OSBC. We therefore applaud the intent of the discussion paper, and encourage its prompt implementation.

But just as we acknowledge that public procurement reforms alone will not deliver a complete solution, we suggest that the informational reforms foreshadowed in the paper are unlikely to affect an end to problematic conduct in the private sector. This is particularly true in relation to the worst-offending businesses.⁵⁴

For this reason, we believe there would be merit in the detailed consideration of potential reforms that would mandate that small businesses be paid within a prescribed timeframe. We note that this approach has attracted the support of a wide cohort of stakeholders, including the Member States of the European Union⁵⁵ and the Australian Small Business and Family Enterprise Ombudsman,⁵⁶ to other small business stakeholders,⁵⁷ and independent analysts.⁵⁸

We acknowledge that any such reform should not be implemented without detailed consideration as to its design. In particular, what represents a reasonable payment timeframe may vary somewhat across industries. The reform might also necessitate a distinct enforcement and dispute resolution regime. But these issues should not be seen as necessarily intractable. That the European Union has already proceeded with implementation should establish that in itself.

We therefore call on the Commonwealth to match its commitment to playing a leadership role in delivering improved payment practices,⁵⁹ by commencing a discussion on mandated payment times.

The Office of the NSW Small Business Commissioner looks forward to playing an active role in any such deliberations, if and when they commence.

To discuss this submission, please contact Thomas Mortimer, Senior Advisor, Advocacy and Strategic Projects, on (02) 8222 4196 or Thomas.Mortimer@smallbusiness.nsw.gov.au. For more information regarding the NSW Government's payment terms reforms, please contact Naushee Rahman, Principal Analyst, Faster Payment Terms, 0477 712 155 or Naushee.Rahman@smallbusiness.nsw.gov.au.

Yours sincerely



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