Octet

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16 July 2021

Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

(Via Committee Secretary)

By email: corporations.joint@aph.gov.au

Dear Committee Members,

Re: Submission to Committee Hearing 28 July – ASIC oversight of supply chain finance

As a significant participant in the Australian supply chain finance industry, Octet Group (Octet) welcomes the opportunity to make a submission to the Committee as part of the abovementioned inquiry.

Unfortunately, supply chain finance is not well understood in Australia and the recent issues associated with Greensill Group risk confusing the picture further. Like other financiers in the supply chain finance industry, Octet is keen that the unique circumstances of Greensill do not prompt a regulatory overreaction that undermines an otherwise well-functioning Australian market that offers clear benefits to small and large participants in the supply chain.

Octet's views and observations on this issue, outlined below, draw on the more than 80 years' combined experience that the Octet founders and principals have in supply chain finance.

Background on the Octet Group

Octet was founded in 2008 by Clive Isenberg and Peter Gammell, who in 1988 were the original founders of Scottish Pacific (now known as ScotPac), a pioneer of supply chain finance in Australia that was eventually acquired by Westpac in 2000.

Today Octet facilitates over $2.5 billion in supply-chain transactions in 68 countries each year. More than 200,000 companies in Australia and overseas transact on the Octet platform.

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Octet's service lines span:

- **Trade Finance** – giving companies involved in supply-chain procurement, including from international suppliers, access to a revolving line of credit to pay suppliers in over 65 countries.
- **Debtor Finance** (often referred to as receivables finance or invoice factoring) – allowing businesses to receive an upfront payment of up to 85% of their outstanding invoices.
- **Supply Chain Accelerate** (often referred to as reverse factoring) – a flexible working capital solution tailored for medium to large Australian businesses. This product allows these businesses to settle 100% of their supplier invoices upfront and pay these invoices 60 or 90 days later, with the cost worn by either party (supplier or buyer) or split as a percentage.

Octet's supply chain finance solutions are designed specifically to ease the working-capital pressures on businesses operating at all points in the supply chain. Participants in Octet's secure platform range in size from annual turnover of $1 million upwards.

For the purposes of the Committee's deliberations, it is Octet's experience as a financier – through our Supply Chain Accelerate product - to larger companies acting as buyers in supply-chain transactions that is most relevant. There are important differences between how Octet deploys this product for the benefit of both large and small businesses, and how other reverse-factoring arrangements are typically structured.

Benefits of supply chain finance (reverse factoring)

Octet firmly believes that reverse factoring, one of the recognised technics of supply chain finance, has an important and beneficial role to play for Australian enterprises (buyers and suppliers/sellers, small and large) in their financial management, specifically their working capital and cashflow.

Depending on the buyer (of goods or services), the cost of reverse factoring or buyer-funded procurement finance to the supplier tends to be *significantly lower* than a bank overdraft (which is usually secured against the company's / director's assets or property).

Importantly, in accessing reverse factoring the seller receives a cashflow benefit via being paid 100% of the invoice value, usually within 30 days of delivery of the goods or services. The buyer benefits by being able to obtain commercially accepted credit terms (with the industry standard being between 30 to 90 days) without any impact on the cashflow of their supplier/seller.

However, reverse factoring only works if all parties, which include the financier, buyer and seller, to the transaction play fair commercially.

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Greensill collapse

Current discussion on possible issues around reverse factoring have unfortunately been clouded by the experience of Greensill.

Reverse factoring models were a subject of criticism – often not well informed – by the media, credit-rating agencies, and small-business advocacy groups well before the collapse of Greensill. And it is a mistake to attribute the collapse of Greensill to the reverse-factoring or buyer-centric procurement funding model. Regulation of certain aspects of Supply Chain Finance should not be reshaped on that basis.

There were several unique features of the Greensill model that set it apart from other supply chain financiers and which, ultimately, contributed to its downfall. These include:

- Greensill, its primary financier Credit Suisse, and its credit insurers Bond & Credit Company, IAG and Tokio Marine, engaged in unacceptable underwriting practices.
- Greensill used trade credit insurance cover as its front-line credit risk process, rather than as a risk-mitigation tool.
- More than half of all outstanding receivables financed by Greensill were for related-party transactions.
- Greensill obtained financing from one of its investors and in turn used this to finance the investor's own poor-performing affiliates.
- According to reports since the collapse, the company seems also to have engaged in aggressive lending against *future* 'receivables' that were expected to arise under *future* purchase orders. This is akin to financing vapor and is not remotely part of traditional reverse factoring.

None of these features of the Greensill model had anything to do with traditional reverse-factoring or buyer-centric procurement funding and would not (and should not) be considered acceptable in a transparent, well-functioning supply chain finance industry.

Broader issues in supply chain finance

Greensill aside, there are other features of reverse factoring, as it is conducted in Australia, that are deserving of scrutiny by the Committee. These include that:

- Many reverse-factoring financiers in Australia (Deutsche Bank, JP Morgan, Greensill, NAB, RBS to name a few) tend to take not only an assignment of the specific receivable from the supplier/seller, but also a General Security Deed over all other receivables of the

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supplier/seller, without the supplier's specific consent. This should not be allowed. The reverse-factoring financier should only be able to take security interest over the specific receivable against which they are providing credit terms and paying the supplier/seller.

- Reverse-factoring financiers typically promise in their marketing to suppliers/sellers that they will be entitled to receive 100% of their invoice value immediately once the transaction occurs. However, they often fail to mention that the buyer must first inspect and approve the goods being transacted. This process can take up to 20 days and then there is a delay of two to three days before funds hit the supplier's bank account. Transparency in representations to suppliers should be mandatory.

- The imbalance in the power relationship between (large) buyers and (smaller) suppliers/sellers means that many suppliers are often unfairly forced into the reverse-factoring arrangement by both the buyer and the supply-chain financier working in tandem. That is because the supplier is generally told the alternative to the reverse-factoring arrangement is an onerous fee of 3% of the invoice value on payment at 60 days.

- Reverse-factoring financiers offer buyers credit terms well beyond the industry norm of 30 to 90 days.

Octet would welcome the opportunity to expand on the points raised in this submission in personal testimony to the Committee on 28 July.

Yours sincerely

Clive Isenberg
Founder and CEO
Octet Finance