The Senate

Foreign Affairs, Defence and Trade Legislation Committee

Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014 [Provisions]

February 2015

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Members of the committee

Core members

Senator Chris Back, LP, WA (Chair)
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Ms Shennia Spillane, Senior Research Officer
Ms Kimberley Balaga, Research Officer
Ms Megan Jones, Administrative Officer

Senate Foreign Affairs, Defence and Trade Committee
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Phone: + 61 2 6277 3535
Fax: + 61 2 6277 5818
Email: fadt.sen@aph.gov.au
Internet: http://www.aph.gov.au/senate_fadt

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Chapter 1
Introduction

Referral of the bill

1.1 On 27 November 2014, the Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014 was referred to the Foreign Affairs, Defence and Trade Legislation Committee for inquiry and report by 11 February 2015.[1]

1.2 The reasons for the referral of the bill, as cited by the Selection of Bills Committee, were 'to consider the principal issues of the impact of substantially expanding the scope of the Export Finance and Insurance Corporation (Efic) and its consequences in relation to aid spending.'[2]

1.3 The Minister for Small Business, the Hon Bruce Billson MP, introduced the bill into the House of Representatives on 22 October 2014.[3]

Conduct of inquiry

1.4 The committee advertised the inquiry on its website. The committee also wrote to individuals and organisations likely to have an interest in the bill, drawing their attention to the inquiry and inviting them to make written submissions.

1.5 The committee received 11 submissions to the inquiry. These submissions are listed at Appendix 1, and are available on the committee's website: www.aph.gov.au/senate_fadt.

Scrutiny by other committees

Scrutiny of Bills Committee

1.6 The Scrutiny of Bills Committee considered the bill according to its usual scrutiny process and did not have comments in relation to the scrutiny principles outlined in Senate Standing Order 24.[4]

Parliamentary Joint Committee on Human Rights

1.7 The Parliamentary Joint Committee on Human Rights examined the bill and considered that the bill does not give rise to any human rights concerns.[5]

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1 *Journals of the Senate*, 27 November 2014, p. 1899.

2 Senate Selection of Bills Committee, *Report 15 of 2014*, 27 November 2014, Appendix 2.

3 House of Representatives, *Votes and Proceedings*, 22 October 2014, p. 899.

4 Scrutiny of Bills Committee, *Alert Digest No. 15 of 2014*, 19 November 2014, p. 42.

5 Parliamentary Joint Committee on Human Rights, Fifteenth Report of the 44th Parliament, p. 8.

Structure of report

1.8 Chapter 2 provides an overview of the bill. Chapter 3 summarises the main issues raised in evidence and contains the committee's view and recommendation.

Acknowledgements

1.9 The committee acknowledges the short period of time available for those who made submissions. The committee thanks all those who assisted with the inquiry.

Chapter 2
Overview of the bill

2.1 The Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014 (the bill) expands Efic's current powers under the *Export Finance and Insurance Corporation Act 1991* (the Act).

2.2 The purpose of the bill is to:

- allow Efic to provide direct loans for export transactions involving all goods (not just capital goods);
- extend the competitive neutrality arrangements under the Efic Act to cover all of Efic's operations;[1] and
- make minor technical amendments.[2]

2.3 During his second reading speech, the Minister for Small Business, the Hon Bruce Billson MP, explained the rationale for the bill:

> The Abbott government recognises the importance of finance as the oxygen of enterprise to small business and is refocusing Efic to increase its capacity to finance small- and medium-sized businesses seeking to capitalise on global trade opportunities. The vast majority of Australia's exporters are small- and medium-sized enterprises, but traditionally they find it more difficult to secure export finance through banks, particularly when exporting to emerging markets…Australian Bureau of Statistics data shows that only five per cent of Australian goods exports are capital goods. And yet, under the current Efic Act, Efic can lend directly in support of capital goods but not all goods. This means Efic cannot lend for exports of many of the products in which Australia excels, like pharmaceuticals, or consumer goods like food and wine. For example, this means Efic can support the export of cows, but not milk…This amendment will also support the government's deregulation agenda and benefit exporters by reducing the time and paperwork required to access Efic support. The new direct lending arrangements will remove the need for exporters of non-capital goods to obtain a guarantee from Efic before they can secure funds from a bank, which doubles the due diligence processing time and requires two sets of documentation and legal fees.[3]

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1 Explanatory Memorandum, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill*, p. 2.

2 T Dale, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014*, Bills Digest No. 55, 2014–15, Parliamentary Library, 25 November 2014, p. 3.

3 The Hon Bruce Billson MP, Minister for Small Business, *House of Representatives Hansard*, 22 October 2014, p. 11615.

2.4 The key provisions of the bill are contained in five items of Schedule 1 and three items of Schedule 2.

2.5 In Schedule 1, a number of minor technical amendments are made in Items 1, 2 and 5 by inserting descriptive titles of subsections. Substantive changes are made in Items 3 and 4, which remove the requirement that Efic can only provide direct loans to exporters of capital goods. Item 3 changes the definition of an ‘eligible transaction’ by replacing ‘capital goods’ with ‘goods’ and Item 4 repeals the definition of ‘capital goods’.

2.6 Schedule 2 of the bill enables the Minister to specify a number of payments Efic must make to the Commonwealth in order to achieve competitive neutrality. These include a debt neutrality charge, guarantee fees and tax-equivalent payments.[4] Competitive neutrality aims to promote healthy competition between public and private businesses by minimising the competitive advantage government businesses may have over private sector financiers due to their Government ownership. This reflects a recommendation made by the Productivity Commission in its 2012 inquiry into Efic.[5]

Financial impact

2.7 While the Explanatory Memorandum states that the bill 'will have no direct financial impact', it may have indirect implications for the Commonwealth in two ways:

- the Commonwealth Government funds Efic directly through providing capital and also guarantees its borrowings. Changes to Efic's operations may impact on Efic’s costs or profits, in turn impacting on the costs or benefits it provides to the Commonwealth; and
- Schedule 2 of the bill broadens the competitive neutrality requirement, creating the capacity for increased cash-flow from Efic to the Commonwealth.[6]

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4 T Dale, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014*, Bills Digest No. 55, 2014–15, Parliamentary Library, 25 November 2014, p. 2.

5 Productivity Commission, *Australia's Export Credit Arrangements*, 31 May 2012, p. 35.

6 Explanatory Memorandum, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill*, p. 2.

Chapter 3

Issues and committee view

Background

3.1 The Export Finance and Insurance Corporation (Efic) was established by the *Export Finance and Insurance Corporation Act 1991* to act as Australia's export credit agency. It is a self-funding statutory authority under the *Public Governance, Performance and Accountability Act 2013*. Efic exists to support the growth of Australian businesses internationally. It does this by providing financial solutions, risk management options and professional advice when the private market is unable or unwilling to do so. This is referred to as Efic's market gap mandate.[1] The Efic website states that Efic 's primary purpose is to:

> …facilitate and encourage Australian export trade on a commercial basis…specifically, by providing financial services in circumstances where they have been unable to source adequate finance from the private sector. We do not compete with the private sector.[2]

3.2 Efic provides financial support to exporters on one of two accounts: the Commercial Account (CA) and the National Interest Account (NIA). The CA operates on a commercial basis with Efic's Board determining whether or not to support particular transactions. The NIA is managed by Efic on behalf of the Australian Government. Decisions about transactions on the NIA are made by Government and then managed by Efic.[3]

3.3 In September 2011, the Labor Government announced a Productivity Commission inquiry into Efic.[4] During the inquiry, Efic argued for an amendment which would allow it to provide direct loans in support of non-capital goods exports.[5] However, the Productivity Commission recommended against this change.[6]

3.4 The Labor Government accepted a number of the Commission's recommendations in its response to the inquiry, and introduced two bills to amend the

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1 Department Foreign Affairs and Trade, *Submission 8*, p. 2.

2 T Dale, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014*, Bills Digest No. 55, 2014–15, Parliamentary Library, 25 November 2014, p. 3.

3 Department Foreign Affairs and Trade, *Submission 8*, p. 2.

4 C Emerson (Minister for Trade) and B Shorten (Assistant Treasurer), *Productivity Commission inquiry into the Export Finance and Insurance Corporation* , Media Release, 1 September 2011.

5 Productivity Commission, *Australia's Export Credit Arrangements*, 31 May 2012, p. 280.

6 Productivity Commission, *Australia's Export Credit Arrangements*, 31 May 2012, pp 35–41.

Act. The first was passed and received Royal Assent to become the *Export Finance and Insurance Corporation Amendment (Finance) Act 2013*.[7]

3.5 A second bill, the Export Finance and Insurance Corporation Amendment (New Mandate and Other Measures) Bill 2013, was introduced but lapsed at the end of the 43rd Parliament. The 2013 bill included a number of changes to the Act which were intended to:

- restrict Efic's operations to areas where there was a clear market failure;
- ensure it focused its activities on small to medium enterprises; and
- extend competitive neutrality to all of Efic's activities (the provisions were similar to those included in the current bill). [8]

3.6 The Abbott Government took the opportunity to review Efic's mandate and operations in the light of developments in the Australian economy and the Government's economic agenda. In doing so, it took into consideration the findings of the 2012 Productivity Commission review of Efic, the Commission of Audit and the preliminary findings of the Murray Financial System Inquiry.[9] The result was a $200 million injection of capital in the 2013–14 Budget.

Current issues facing SMEs

3.7 The vast majority of Australian exporters are small and medium sized enterprises (SMEs). Market data sourced by Efic shows there are 44,000 exporters in Australia and most of these exporters (34,000) have sales of less than $5 million per year. Due to the small size of most SME ventures, the return on a bank's investment is often considered too low to warrant the transaction.[10] Requests made for assistance to Efic are assessed on the basis of the commercial viability of the exporter as well as evidence of the market's inability to provide the financial solution required.[11] However, Efic's current lending scope is narrow, with capital goods exports constituting only five per cent of all Australian exports.[12]

3.8 Exporters which are eligible for assistance from Efic face a number of further issues, including:

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7 T Dale, *Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014*, Bills Digest No. 55, 2014–15, Parliamentary Library, 25 November 2014, p. 3.

8 E Karanikolas and J Murphy, *Export Finance and Insurance Corporation Amendment (New Mandate and Other Measures) Bill 2013*, Bills Digest No. 131, 2012–13, Parliamentary Library, 25 November 2014, p. 3.

9 Department Foreign Affairs and Trade, *Submission 8*, p. 4.

10 Department Foreign Affairs and Trade, *Submission 8*, p. 2.

11 Department Foreign Affairs and Trade, *Submission 8*, pp 2–3.

12 Export Council of Australia, *Submission 1*, p. 2.

- delays due to administrative burdens;[13]
- complexity in dealing with more than one party;[14]
- duplication of costs;[15] and
- the antiquated Export Working Capital Guarantee Scheme.[16]

3.9 Several submitters acknowledged Efic's essential support in assisting their companies to win overseas contracts, and expressed enthusiasm for further improvement including support for the bill.[17] The main issues raised in evidence were summarised by the Export Council of Australia submission:

> In response to the most recent inquiry, the ECA would like to reiterate the important role EFIC plays in providing finance to Australian exporters and express its strong support for increasing the flexibility of EFIC's lending arrangements to include the ability to lend directly to all SMEs…[Australian International Business Survey] research….and other surveys conducted over recent years, have all highlighted difficulties that SME businesses have experienced in accessing working capital/finance to take advantage of export opportunities…With only 5% of exports from Australia being capital goods, EFIC's scope to lend is currently narrow. Amending the Act will expand EFIC's capacity to support Australian business, particularly SMEs.
>
> Amending the EFIC Act to allow EFIC the flexibility to lend directly will lead to a reduction in the amount of paperwork required, and therefore the processing time for a transaction, which is essential given the fast-paced nature of business. Reducing the administrative processes will result in lower costs that will ultimately make EFIC's services more efficient for SMEs. Improving the efficiency of EFIC's services will mean that those business that are not able to access finance through the commercial banking system, will have a viable alternative to seek access to finance.[18]

3.10 The submission from Camatic Pty Ltd, a major supplier of cinema, stadium and educational seating worldwide, made a similar argument:

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13 Export Council of Australia, *Submission 1*, p. 2; name withheld, *Submission 4*, p. 2; Access Innovation Media Pty Ltd, *Submission 9*, p. 2; Camatic Pty Ltd, *Submission 11*, p. 2.

14 South State Food & Beverage Pty Ltd**,** *Submission 2*, p. 1; ANCA Pty Ltd, *Submission 3*, p. 1; name withheld, *Submission 4*, p. 1; Camatic Pty Ltd, *Submission 11*, p. 2.

15 ANCA Pty Ltd, *Submission 3*, p. 1; name withheld, *Submission 4*, p. 1; Access Innovation Media Pty Ltd, *Submission 9*, p. 2; Ferra Engineering Pty Ltd, *Submission 10*, p. 2.

16 South State Food & Beverage Pty Ltd**,** *Submission 2*, p. 1; ANCA Pty Ltd, *Submission 3*, p. 1; name withheld, *Submission 4*, p. 1.

17 Export Council of Australia, *Submission 1*, p. 2; South State Food & Beverage Pty Ltd**,** *Submission 2*, p. 1; ANCA Pty Ltd, *Submission 3*, p. 1; name withheld, *Submission 4*, p. 1; OM Engineering, *Submission 5*, p. 2; Quickstep Technologies, *Submission 6*, p. 2; Australian Chamber of Commerce and Industry, *Submission 7*, p. 1; Ferra Engineering Pty Ltd, *Submission 10*, p. 2; Camatic Pty Ltd, *Submission 11*, p. 2.

18 Export Council of Australia, *Submission 1*, p. 2.

> Obtaining additional short term funding from banks for international projects, is a difficult process for private companies with limited working capital. When some form of facility is eventually provided, the time taken can often be outside of an acceptable timeframe for the contract at hand. The additional complexity of working with two parties (bank for facility and EFIC as the security provider) can be tedious and require extended timeframes, that are often not available. These issues do not exist for Camatic's opposition who are often based in the country that we are tendering. For Camatic to be able to deal directly with EFIC as a direct lending facility, there would be several significant advantages, being:
>
> - increased business from short term lending against contracts; (Assuming some form of approved facility remains in place);
> - improved time frames to provide clients with security required;
> - improved trade facilities for larger projects;
> - less complexity in dealing with more than one party; and
> - increased business through more competitive pricing.
>
> Camatic have had a terrific working relationship with EFIC for many years now. Where the process has not always been easy, without it Camatic would not be as internationally recognised today as we are. Camatic see some great benefits in being able to borrow directly from EFIC and we would expect it will make our task of growing international business successful.[19]

Reduced lending costs and improved administrative processes

3.11 A number of submitters argued that private companies would benefit significantly from reduced lending costs, streamlined administrative procedures and ultimately reduced costs to consumers as a result of the amendments in the bill. The submission from Ferra Engineering argued that:

> Direct lending will enable reduced lending cost which ultimately decreases cost to the consumer and increase value of products being sold. Currently all companies using EFIC pay a margin to their lender as well as a margin to EFIC. They also pay an establishment cost to EFIC as well as an establishment cost to their incumbent bank. The overall position is a double up in fees and interest rate margins dependent on company risk profile that global customers will not pay for.[20]

3.12 Australian SMEs are at a disadvantage when competing against US or European companies with access to faster and cheaper funding.[21] The Export Working Capital Scheme aims to provide financiers with the necessary Efic guarantees to allow them to release funding. However, some exporters have experienced doubling up of certain costs and processes, such as documentation, approvals and fees, and have

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19 Camatic Pty Ltd, *Submission 11*, p. 2.

20 Ferra Engineering Pty Ltd, *Submission 10*, p. 2.

21 Ferra Engineering Pty Ltd, *Submission 10*, p. 2.

argued that the scheme provides an antiquated mechanism to assist SMEs with funding.[22]

3.13 One Melbourne manufacturer of tool grinders, ANCA Pty Ltd, with facilities in Thailand and Taiwan and distribution centres in Asia, Europe and the United States, described in its submissions how the company had twice used Efic's support in winning two significant export contracts. This came through an Export Working Capital Guarantee to ANCA's bank which helped fund the supply and purchase agreement:

> In both instances EFIC, ANCA and the bank worked well together but the process involved was time consuming and ANCA did incur some duplication of costs and fees in order to get the funds and the guarantee in place.
>
> The proposed changes [in the bill] would simplify the process and provide ANCA greater certainty, flexibility and agility in targeting and winning major export contracts. It will give ANCA an edge particularly in emerging markets over our competitors…[23]

3.14 South State Food & Beverage Pty Ltd described a similar experience gaining access to Efic funds through the Export Working Capital Guarantee Scheme:

> First impressions of the working capital guarantee facility were impressive, however as we moved toward our application we realised that the application to enter the scheme was not only time consuming but laborious for our business and involved incredible scrutiny from both EFIC and our bankers. Quite honestly, the effort required to gain approval was unbelievably bureaucratic and costly requiring hours of senior management time. Now we have the ongoing reporting and maintenance of the facility to deal with instead of focusing our efforts on what we do best, selling product… I would support 100% the implementation of a scheme by EFIC that allowed them to loan directly to companies such as ours, thus removing the banks input and laborious costly and less efficient, some would say 'antiquated' Working Capital Guarantee scheme. It would certainly allow us to plan any future expansion with a great deal of confidence, as I'm not sure I would bother again with the existing scheme as we are paying both EFIC and our bank for the pleasure as opposed to channelling those funds into the promotion and expansion of our business to the global market.[24]

3.15 Similar observations were made by a second submitter who also noted the Scheme's duplication of costs under Efic's guarantee scheme:

> …additional funding was required in order to allow our company to purchase the required materials to manufacture the products in demand. Unable to source the appropriate funding from our existing financiers for this purpose, we approached the Export Finance and Insurance Corporation

22 Name withheld, *Submission 4*, p. 1.

23 ANCA Pty Ltd, *Submission 3*, p. 2.

24 South State Food & Beverage Pty Ltd**,** *Submission 2*, p. 1.

> (EFIC). Through their Export Working Capital Guarantee facility, were able to provide the required guarantee to our existing financiers which in turn allowed them to provide us $AUD600, 000 in ongoing funding, for the purpose of acquiring the necessary raw materials. This facility 'dove-tails' with our financiers requirements, and provides them the necessary Efic guarantees to allow them to release the funding required by this company for the additional export sales. By undergoing this funding exercise (and excluding costs associated with Efic's initial due diligence process of our company) we have experienced 'doubling-up' of the following activities and costs by Efic and our financiers;
>
> (a) regular Annual Credit Approvals;
>
> (b) documents and information etc for both EFIC and Financiers;
>
> (c) ongoing facility fees for both EFIC and our financiers;
>
> (d) ongoing approvals required for every transaction within the $600,000 funding limit;
>
> (e) notification of draw down amounts and reports for every transaction and reliance on communication lines between EFIC and the financier.[25]

Competitive neutrality

3.16 As a measure to ensure that direct lending changes do not bring Efic into direct competition with private sector financiers, Schedule 2 includes competitive neutrality principles which require Efic to pay a debt neutrality charge or guarantee fee and a tax equivalent payment as determined appropriate by the minister.[26]

3.17 While the majority of submissions strongly support the bill, the committee notes the concern expressed by Ferra Engineering Pty Ltd with regards to the competitive neutrality aspect of the bill. The submission from Ferra Engineering cautioned that changes should not be made to competitive neutrality at the present time:[27]

> In theory the recommendation has sound logic but in the real world SME's with limited access to finance will be affected by this proposal. Schedule 2 - Competitive Neutrality will effectively nullify any advantage Australian SME's would get compared to larger corporations with access to cheaper capital. Ferra recommends the government reviews competitive neutrality with a view on how this proposal will affect SME's as they will form the bulk of the lending base needing assistance.[28]

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25 Name withheld, *Submission 4*, p. 1.

26 Department Foreign Affairs and Trade, *Submission 8*, p. 4.

27 Ferra Engineering Pty Ltd, *Submission 10*, p. 3.

28 Ferra Engineering Pty Ltd, *Submission 10*, p. 3.

Aid considerations

3.18 The committee notes evidence from the Department of Foreign Affairs and Trade that expanding the scope of Efic as proposed by the bill will not have any consequences in relation to Australia's aid program:

> While some exports or projects supported by EFIC may contribute to developmental outcomes, the financial solutions provided by EFIC on its commercial account are not part of Australia's aid program. Decisions to provide financial solutions on EFIC's commercial account are based on commercial assessments by EFIC, in line with EFIC's Credit Guidelines and Policy and Procedure for Environmental and Social Review of Transactions.[29]

3.19 The department's submission noted that Part 2, Section 7(c) of the Efic Act provides that one of Efic's functions is to administer payments under export contracts with respect to overseas aid projects. However, this provision relates to the ongoing management of long–term exposures generated under the Australian Government's Development Import Finance Facility which was introduced in 1980 and discontinued in 1996.[30]

Committee view

3.20 The committee's inquiry received support for passage of the bill from all submitters.[31] A range of stakeholders were represented in evidence to the committee, including the Export Council of Australia, the Australian Chamber of Commerce and Industry, private SMEs and the Department of Foreign Affairs and Trade.

3.21 The committee recognises that increasing Efic's lending ability to all types of goods will offer a viable alternative for SMEs seeking access to finance for export growth opportunities. The bill will assist smaller exporters who may be excluded by banks due to the lower dollar values of their transactions.

3.22 The committee considers that the amendments proposed by the bill will significantly improve Efic's lending arrangements, and reduce the excessive cost and administrative burden currently experienced by the majority of Australia's SME exporters. Australian companies will also benefit from these improvements through more competitive pricing and reduced processing times. For these reasons, the committee supports passage of the bill through the parliament unamended.

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29 Department Foreign Affairs and Trade, *Submission 8*, p. 5.

30 Department Foreign Affairs and Trade, *Submission 8*, p. 5.

31 Export Council of Australia, *Submission 1*, p. 2; South State Food & Beverage Pty Ltd**,** *Submission 2*, p. 1, ANCA Pty Ltd, *Submission 3*, p. 1; name withheld, *Submission 4*, p. 2; Quickstep Technologies, *Submission 6*, p. 2; Department of Foreign Affairs and Trade, *Submission 8*, p. 2; Access Innovation Media Pty Ltd, *Submission 9*, p. 2; Ferra Engineering Pty Ltd, *Submission 10*, p. 3; Camatic Pty Ltd, *Submission 11*, p. 2.

Recommendation 1

3.23 The committee recommends that the Senate pass the Export Finance and Insurance Corporation Amendment (Direct Lending and Other Measures) Bill 2014.

Senator Chris Back
Chair

Appendix 1

Public submissions

1 Export Council of Australia

2 South State Food & Beverage

3 ANCA Pty Ltd

4 Name withheld

5 OM Engineering Pty Ltd

6 Quickstep Technologies Pty Ltd

7 Australia Chamber of Commerce and Industry

8 Department of Foreign Affairs and Trade

9 Access Innovation Media Pty Limited

10 Ferra Engineering Pty Ltd

11 Camatic Pty Ltd

Additional information

1 Letter from The Hon Andrew Robb AO MP, Minister for Trade and Investment, received 10 February 2015.