Australian Government

Department of Industry, Innovation, Climate Change, Science, Research and Tertiary Education

Australian Prompt Payment Protocol Discussion Paper

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Consultation Process

Request for feedback

The Government is seeking your feedback and comments on the proposed introduction of a Prompt Payment Protocol in Australia. Feedback and comments received will help to inform the development and implementation.

While submissions may be by post, electronic lodgement is preferred. For accessibility reasons, please email responses in a Word or RTF format. You are welcome to submit an additional PDF version.

Closing date for feedback: 23 August 2013

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Foreword

We are pleased to release for comment this discussion paper seeking stakeholder views on an Australian Prompt Payment Protocol to help strengthen small business payment terms, cash flow and business-to-business relationships.

In the current economic climate, small businesses are facing the challenges of global economic uncertainty, the high Australian dollar and tight cash flow. Cash flow in particular is essential to the prosperity and health of small businesses. Late payments between businesses have a negative impact on competitiveness and increase the cost of doing business. Conversely, on time payments help businesses to unlock greater opportunities for investment to grow their business and to pursue their entrepreneurial aspirations.

The voluntary Prompt Payment Protocol targets business-to-business late payments without introducing extra regulation. The Protocol will not only encourage companies to publicly commit to paying on time, but enable small businesses to leverage better contracting behaviours and strengthen overall business relationships. Paying on time also offers buyers and sellers a simple method of injecting liquidity into their supply chains.

This paper outlines the key design features of the Protocol that will help encourage a necessary shift in Australia's late payment culture. It canvasses a range of implementation options to ensure the Protocol is capable of delivering real benefits to business.

The Rudd Government is committed to ensuring the ongoing health and growth of Australia's vibrant small business sector. Your feedback will help shape this new initiative for enhancing the operating environment for all businesses.

The Hon Gary Gray AO MP
Minister for Small Business

The Hon Bernie Ripoll MP
Parliamentary Secretary for Small Business

Executive Summary

The Australian Government is considering the introduction of a voluntary Prompt Payment Protocol ('the Protocol') to tackle delays in trade payments between businesses, particularly late payments to small business.

Business-to-business late payments are a significant source of cash flow problems. Dun & Bradstreet estimates that a staggering **$19 billion** annually is locked away from businesses beyond the widely accepted 30 day payment term. Late payment also adds financial and administrative costs, reduces the potential for investment opportunities, damages business relationships and fuels business uncertainty. This weakening effect on businesses, particularly small businesses, compromises their competitiveness and survival.

The Protocol aims to foster a broad change in Australia's late payment culture by establishing core principles that set the benchmark for good payment practices.

The Protocol Principles

1. Pay on time
2. Communicate clearly
3. Encourage good business relationships
4. Adopt a complaint resolution process
5. Identify yourself as a Prompt Payment Leader

The Government has undertaken initial consultation with a range of key stakeholders, including peak industry and small business groups, financial providers, individual companies and within government. Overall, there was strong business support for further development of an Australian Protocol. Stakeholders expressed a clear need for further public consultation on the Protocol's design features to ensure the benefits can be realised.

The purpose of this paper is to seek feedback on these key design and implementation issues, including suitable core payment principles, administration, participation requirements and compliance measures. Feedback on these important issues will inform Government and help shape this new initiative.

Introduction

From large multinational companies to the local corner store, cash flow is the lifeblood that pumps through the heart of every Australian business. Cash is vital for keeping businesses in business – to pay staff wages, purchase stock, meet tax obligations and invest in new opportunities.

An essential part of managing good cash flow is for businesses to make sure that they are *paid on time*. Late payments can be caused by poor debt collection practices by the creditor business, which can often be a symptom of poor business management. In other cases, despite sound debt collection strategies and best efforts by the business, they can still be left waiting to receive payment for goods and services, particularly when dealing with business customers.

Business-to-business late payments represent a significant cause of cash flow problems. Businesses, particularly large businesses, are taking longer to pay their commercial trade bills with other businesses, contributing to a culture of late payment that has taken hold in Australia. These delays in payment can often have a knock-on effect, being passed down the supply chain to those that can least afford them, often small businesses.

Cash flow is especially important for small businesses that typically operate on tight budgets while facing challenging economic conditions. Maintaining reliable cash flow can mean the difference between success and failure. Dun & Bradstreet estimates that **90 per cent** of small business failures are caused by poor cash flow.

Small businesses represent almost 96 per cent of all businesses in Australia. More than 2 million small businesses keep over 4.8 million Australians employed and contribute around 34 per cent of private sector industry value added or approximately a fifth of Gross Domestic Product (GDP).[1]

Small businesses may face an inherent imbalance of bargaining power when dealing with large companies. They can often be reluctant to challenge or pursue late payments for fear of jeopardising future work.

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[1] www.innovation.gov.au/SmallBusiness/KeyFacts/Pages/default.aspx

In other cases, payment terms may simply be left unspecified in contracts or agreements – leaving small businesses unaware or uncertain of their rights. As a result, there may be instances where late payers are taking advantage of what is effectively an interest free loan arrangement, while suppliers are left cash starved.

Late payments also add to the cost of doing business. Administrative costs associated with late payment recovery processes and financing costs to borrow money needed to cover any subsequent cash shortfalls can further burden small business. This weakening effect on small business liquidity and solvency can in turn dull their ability to compete and grow. Small businesses that are confronted with many late payments are robbed of the capacity to undertake important investment opportunities, such as business improvement through innovation and skills, to increase productivity.

The problem of late payment goes beyond merely a need for businesses to make quicker payments – it is also about payment behaviour. Businesses want reliability and certainty of payment terms, to build enduring and sustainable business relationships.

The Department's research into small business disputes found that the majority of serious disagreements with other businesses related to disputes over payment for goods and services. A public commitment to uphold fundamental payment principles, that underpin reasonable and ethical behaviour, will help nurture a stronger network of suppliers and business partners. In turn, this will build an environment that strengthens business confidence and allows all businesses to flourish.

It is time for Australia to work towards changing its late payment culture.

The introduction of a Prompt Payment Protocol will mark the first step towards this decisive shift. The Government is committed to working with business to address systematic late payments and to help boost opportunities for business innovation, competition and productivity across the economy.

Australia's Trade Payment Environment – Over $19 Billion Locked Up

This section of the paper aims to provide an overview of the late payment situation across the Australian economy. It provides insights into the scale of the problem; the impact on businesses of different sizes and in various sectors; and explores international comparisons on payment performance.

The Department commissioned Dun & Bradstreet, one of Australia's leading sources of commercial credit information, to assist with trade payment data analysis in order to assess Australia's payment environment as a whole.

Culture of late payments in Australia

In the first quarter of 2013, Dun & Bradstreet analysis showed that over 32 per cent of all business payments were made beyond the standard 30 day term. Of even greater concern, almost a third of these late payments were made after 60 days (see Figure 1). Australian businesses took on average **54.1 days** to pay their bills which equates to **$4.84 billion** being withheld from businesses in the first quarter of 2013 alone.

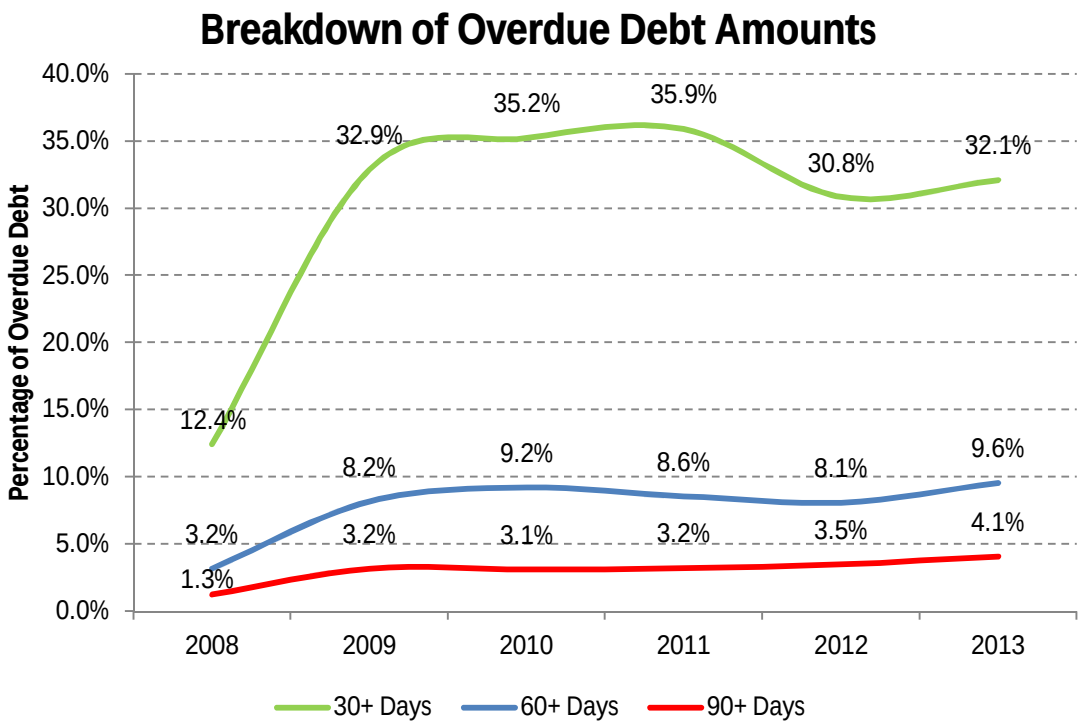
Analysis of trade payments made throughout the 2012 calendar year tells a similar story, with Australian businesses left waiting an overage of **52.3 days** to receive payment. This represents a staggering **$19.18 billion** annually that was withheld from Australian businesses beyond the 30-day payment term.

Indeed, Australia has a concerning history of late payments which have remained consistently high since 2008. The average number of days taken to settle business accounts from 2008 to 2012 has remained at over 50 days. This has amounted to an average of $19.10 billion withheld each year.

Table 1: Yearly breakdown of business payments

Year	Average number of days businesses take to settle accounts	Amount withheld due to late payments
2012	52.3	$19.2 billion
2011	53.3	$21.5 billion
2010	52.4	$17.7 billion
2009	54.0	$18.1 billion
2008	56.3	$17.7 billion

Figure 1:



Company Size

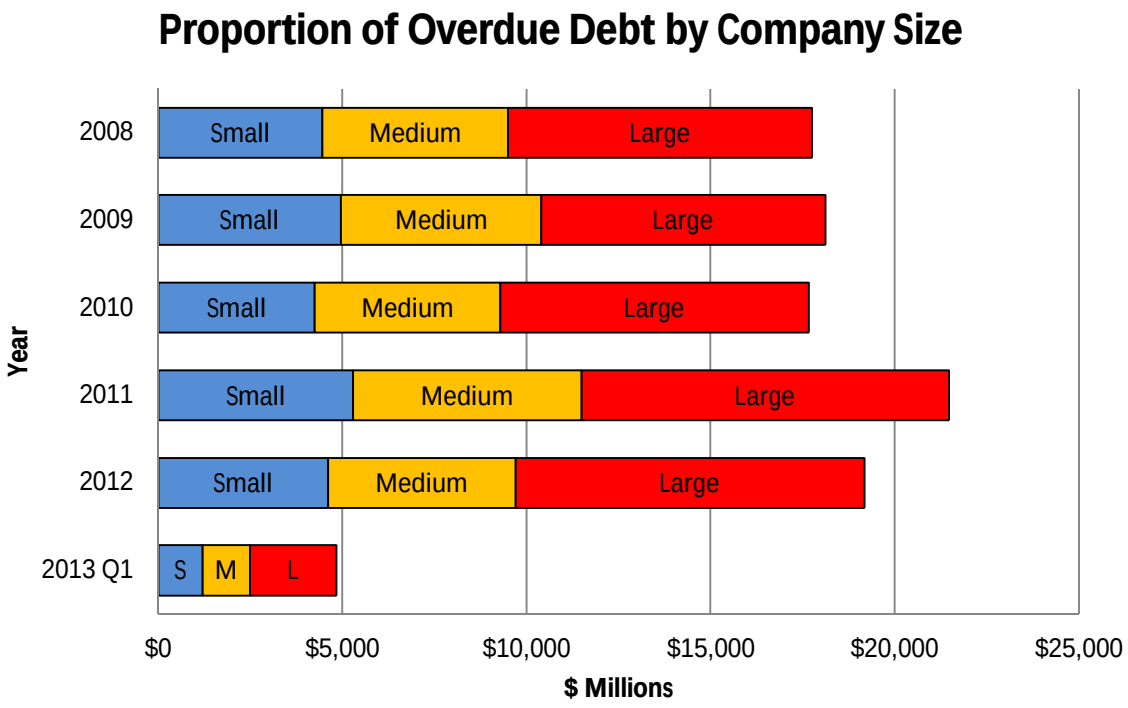
Company size has shown to be a factor in payment performance, with large companies consistently taking longer to pay back debt than smaller companies.

In 2013, large companies (200+ employees) took an average of just over **56 days** to pay their bills, whilst small firms (1-19 employees) took on average **52.5 days**. Medium sized companies (20-199 employees) were the best performers, taking on average just under **50 days** to pay their bills.

Large companies are not only taking the longest to pay their bills, they are also responsible for withholding the most payments in the economy by dollar value (see Figure 2). This is particularly striking given that large companies make up less than 1 per cent of the total number of businesses in Australia.[2]

[2] ABS Cat. No. 8165.0

Figure 2:



Different sized companies often have varying cash flow management strategies. Companies can often receive a discount for paying back credit on time, which presents companies with a trade-off between the cost of credit and the length of time they hold credit.

Some larger companies focus more on managing their cash flow by paying late rather than on the price of that credit. Small businesses, which are generally more price sensitive, will often want to make payments earlier and receive a discount, although their ability to do so can be stymied by the slower payments of other businesses.

Payment delays can often have a domino effect across the broader economy. Delays in payments are typically passed down the supply chain and are often borne by small businesses, which may in turn withhold payments to their staff, suppliers, financiers or the tax office.

This cycle of unhealthy late payments can have serious consequences. Dun & Bradstreet's research suggests that the probability of business failure is significantly higher for those businesses that continually receive late payments.

Based on Dun & Bradstreet's failure score modelling, small businesses that experience late payments are **three times more likely** to close down compared to those that receive payments within 30 days. The problem can take on a very human dimension for small business owners, as often their personal and family finances are closely bound to the fate of their small business.

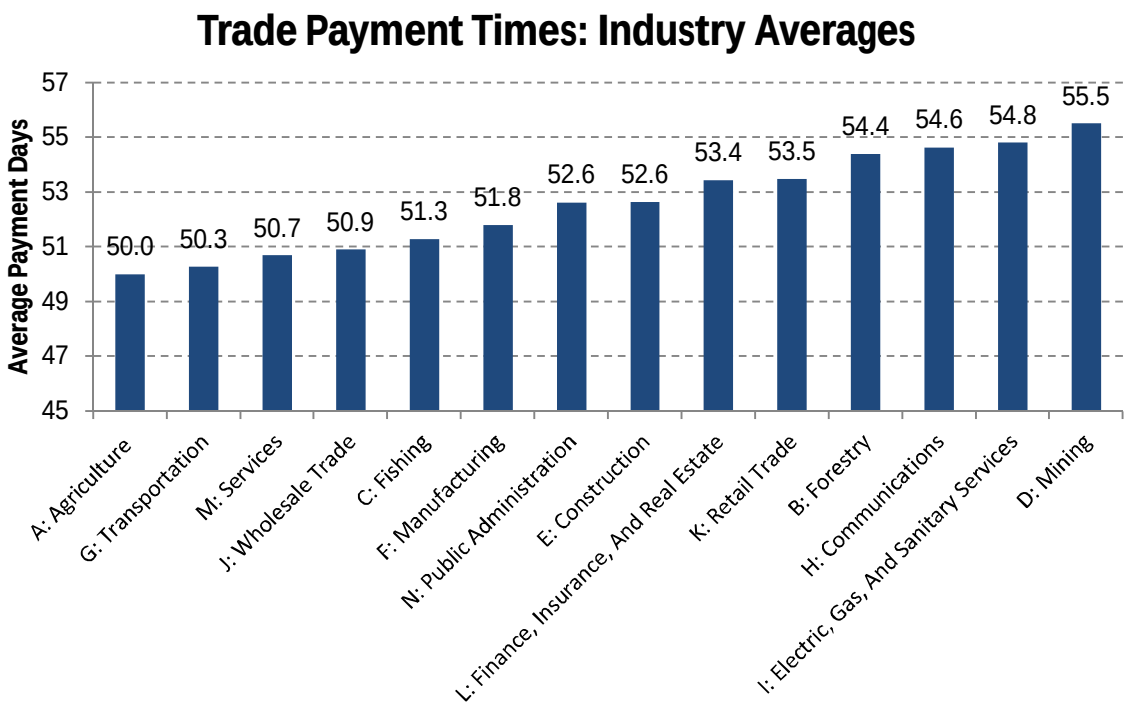
Industry Sectors

Payment performance also differs by industry sectors. Some of Australia's key industries that support innovation and the creation of high-skilled, high-paid jobs are plagued by late business payments.

According to Dun & Bradstreet, the three slowest-to-pay industries in 2012 were mining at an average of 55.5 days; electricity, gas and sanitary services at 54.8 days and communications at 54.6 days.

The three best performing industries in 2012 were agriculture at 50 days and transportation at 50.3 and services at 50.9 days.

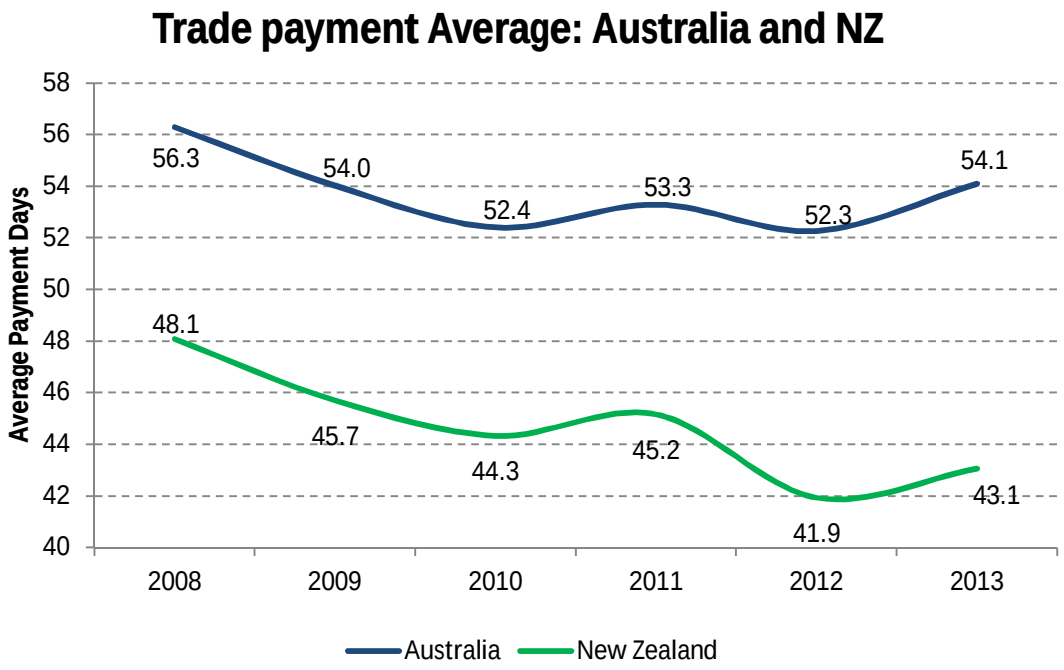
Figure 3:



International Comparisons

Based on Dun & Bradstreet's international trade data, New Zealand business payments have been consistently faster compared to Australia. Since 2008, Australian businesses took an average of 53.7 days to pay its bills, while New Zealand businesses took only 44.7 days. Interestingly, both countries appear to follow similar trends over time, which may suggest similar economic factors at play that influence payment times (see Figure 4). However, Australia's consistently slower payment performance may provide some indication of differing payment cultures that have become ingrained within each country.

Figure 4:



Other research conducted in the United Kingdom suggests that their overall payment times have remained relatively stable since 2008 at 25 Days Beyond Terms. The data indicated that the UK's larger companies were paying on average 14.6 days slower compared to smaller companies in December 2012.[3]

[3] http://press.experian.com/United-Kingdom/Press-Release/prompt-payment-code.aspx

In comparison with other countries, Australia may be lagging behind in terms of prompt payment to business. This means that Australian businesses, particularly small businesses, may be disadvantaged when competing internationally with overseas firms that enjoy a stronger cash flow environment.

Improving Australia's Payment Practices

As Australian small businesses face increasing challenges from a high Australian dollar, structural readjustment pressures and an uncertain global economic outlook, *every dollar paid on time counts*.

The Government's 30 Day Payment Policy, which requires all agencies to pay invoices from small business (up to and including $5 million) within 30 days of receiving a correctly rendered invoice, has dramatically improved Government payment performance over time.[4]

While the Government continues to lead by example, the policy seems to have had no discernible or incentivising effect on private sector payment terms. With more than $19 billion in late payments at stake for business, there is an enormous opportunity to reap the benefits from improving payment terms in the private sector.

Focus Questions

- What are some of the common causes of late payments in these industries?
- What are some of the driving factors that determine late payment in different industries?
- In which industries is the payment relationship between small and large businesses most strained?

[4] http://innovation.gov.au/SmallBusiness/KeyFacts/Pages/default.aspx.

Australian Prompt Payment Protocol

The introduction of a voluntary Prompt Payment Protocol (the Protocol) aims to foster a broad change in Australia's late payment culture. It aims to encourage normative behaviour change across all businesses by focusing attention on reasonable and equitable conduct in relation to payment terms. Over time, it will seek to improve contracting practices and support on-time payment, predictability and certainty for all businesses.

The Protocol will contain fundamental payment principles to set a benchmark for good contracting practices and behaviours. Australian businesses of all sizes, in all sectors, will be encouraged to voluntarily sign up to the Protocol and publicly commit to upholding these principles.

The Protocol will provide a flexible, non-regulatory framework for improving cash flow certainty. The 'Protocol' terminology was adopted in preference to a 'Code' to signify a clear distinction from prescriptive, regulatory-based industry codes of conduct.

The Protocol does not encroach on the freedom of contracting between businesses. It focuses on promoting core principles and avoids being overly prescriptive. Significantly, it does not attempt to specify fixed payment times (such as 30 days) across all businesses. This recognises that what is considered 'prompt payment' may vary significantly between industries.

The standard 30 day payment term, a historic convention that arose long before the advent of modern payment technology and processes, should not necessarily be used to judge prompt payment. In many industries, there is no reason why significantly shorter payment times would not be achievable.

The following principles have been modelled on the UK Prompt Payment Code and may serve as the basis for shaping Australia's approach to improving payment terms.

The Protocol Principles

The Protocol includes five fundamental principles:

1. Pay on time

- Pay business suppliers on time within agreed terms set at the outset of the contract;
- Do not change payment terms unilaterally or retrospectively;
- Do not change the length of payment for smaller companies on unreasonable grounds.

2. Communicate clearly

- Write contract payment terms in clear and simple language;
- Give suppliers clear guidance on payment terms and procedures;
- Inform suppliers of access to internal complaints and disputes systems if available;
- Promptly advise suppliers if there is a reason why an invoice will not be paid within the agreed terms.

3. Encourage good business relationships

- Encourage suppliers to adopt the Protocol in their own supply chains;

4. Adopt a complaint resolution process

- Adopt a process for reviewing complaints and resolving disputes;
- Respond to the complaint or dispute as quickly as possible.

5. Identify yourself as a prompt payment leader

- Have the choice of using Prompt Payment Protocol branding (co-endorsed by business and Government) to inform others of your prompt payment commitment.

Focus Questions

- Are there any fundamental challenges associated with these principles and why?
- Are there other fundamental principles that should be included?
- Are there any issues in business-to-business payment processes that these principles do not cover?

The Benefits

The Protocol will be a new feature in Australia's trade payment environment that will deliver benefits across the whole economy.

Its broad base, long-term approach to encouraging on-time payments will facilitate cash flow through the economy and open greater opportunities for business investment and growth, strengthen competitiveness and solvency, and lift business confidence. It will help build trust and enduring business relationships, which in turn may lead to fewer business-to-business disputes.

The Protocol has been designed to align with these key commercial drivers for business success in order to generate voluntary support across Australia.

Small Business Benefits

Small businesses will benefit from the introduction of the Protocol in several practical ways. The introduction of the Protocol itself will raise small business awareness of the importance of establishing clear and transparent payment terms and expectations at the outset of contracts and agreements.

The Protocol will provide a means for small businesses to identify other businesses that are committed to paying them promptly. In particular, small businesses will gain confidence in dealing with larger businesses that become signatories to the Protocol, with greater certainty that they will be paid on-time and treated reasonably in accordance with the Protocol.

As seen in the United Kingdom (UK), as support for the Protocol builds momentum and major companies help champion the initiative, it should generate a strong community expectation for companies to participate. Late payers may become increasingly conspicuous in their absence from the Protocol and may face greater public scrutiny in regard to their payment practices. This may exert pressure on late payers to participate in the Protocol and lift their game, or at the very least, may help bring the issue to the forefront of their business dealings.

Large businesses that fail to honour their promise may be held publicly accountable and possibly removed as a signatory. In this way, the Protocol will help small businesses to leverage their bargaining position and empower them to refer to the Protocol as a baseline for negotiation on payment terms.

Over time, this will help ease pressures on cash flow - minimising a key factor in small business failure. Addressing late payments will also help to reduce the cost of doing business by minimising the administrative and financial costs associated with late payments.

The Protocol will help establish the framework for resolving business disputes that relate to payment conduct. The Department's 2010 survey on small business disputes found that of the small businesses surveyed, and found to have experienced a serious disagreement, most of these (65 per cent) involved a dispute over payment for goods and services.[5] Furthermore, the research showed that small businesses tend to avoid dealing with disputes until it has reached a toxic stage. The Protocol will act as a preventative measure to help avoid or resolve disputes before permanent damage is inflicted on the business relationship.

The Protocol will not improve small business cash flow overnight. International experience shows that it may take several years for the Protocol to have an effect. However, the Protocol represents an important part of the longer term approach to encourage prompt payment to business.

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[5] http://www.innovation.gov.au/SmallBusiness/KeyFacts/Pages/default.aspx

Large Business Benefits

Large businesses that become signatories to the Protocol will be able to gain reputational benefits by strengthening their corporate image and community standing as good corporate citizens. The general community is likely to support and value businesses that demonstrate a real commitment to ethical and sustainable payment practices, particularly in their dealings with small businesses.

Prompt Payment Logo and Marketing

To maximise the incentive and benefit for businesses that sign up, a key feature of the Protocol will include branding and a logo, co-endorsed by business and Government, to identify signatories to the Protocol. Similar in principle to the Heart Foundation's tick of approval or the Buy Australian logo, prominent branding will be developed to allow signatories to identify and promote themselves as business leaders in prompt payment.

Preliminary consultation with key stakeholders has indicated strong support for this marketing and promotional element, which may be a key factor for driving widespread take-up of the Protocol.

In conjunction with the logo, a Prompt Payment Protocol website will be developed. The website will be a central source of information about the Protocol, including the Protocol's principles; requirements for becoming a signatory; a list of current signatories; further information on sound contracting practices; and case studies.

Build Stronger Business Relationships

Great companies understand that success is not measured just in terms of short term profits and bottom line figures, but also in terms of how the company can establish the best conditions to allow it to flourish over time. These corporate leaders deliver more than just financial returns, they also build enduring institutions.

Apart from distinguishing themselves from their competitors, the Protocol also allows larger businesses to identify and attract other like-minded partners and suppliers that share their corporate values. Initial stakeholder feedback has noted that large businesses want to be able to identify and work with other prompt paying businesses, regardless of size.

Large businesses can use the Protocol to build trust and strengthen business relationships throughout their supply chains. In highly competitive industries, large businesses want to attract the best small business partners that are often capable of securing a significant proportion of company revenue. The Protocol's marketing feature also offers large businesses a cost effective way to promote their brand values and goodwill across the small business community.

The problem of late payments often has a domino effect and it only takes one party within the supply chain to cause significant delays. The Protocol's principle of encouraging others in the supply chain to commit to prompt payment will strengthen the financial position of the supply base by supporting greater overall efficiency and reliability in the system.

Case Study: UK Prompt Payment Code

In the United Kingdom, a Prompt Payment Code was introduced in 2008 to improve trade payments. Reports from the UK suggest the Prompt Payment Code has had a positive effect on payment times in the four years since its launch, with signatories now paying on average 12 days quicker than in December 2008. It was also found that on average signatories to the Code paid five days earlier than non-signatories. This indicates a positive outcome, and a real shift in payment culture. The UK's larger companies in particular have made significant progress in terms of improvement to their payment times. Furthermore, independent analysis suggests that current signatories to the Code represent over 60 per cent of total UK supply chain value.

Based on the UK model, it is envisaged that the Protocol will attract signatories across all sectors, including from multinational corporations, small and medium sized enterprises, major banks, federal and state government departments and agencies, and local councils.

Transforming Protocol Principles into Action

A further element of the Protocol will involve building a bridge between the core payment principles and the practical tools to convert the Protocol into action. This feature aims to improve upon the UK model, to allow the Protocol to evolve to meet the challenges and opportunities of a fast-changing business environment and rapid advancements in technology.

The Government's investment in the National Broadband Network will provide opportunities for businesses to develop and adopt new innovative payment systems and processes to support faster payments to business.

The administration of the Protocol could involve ongoing work to identify linkages to other industry and government initiatives that businesses can adopt or incorporate into their organisation to help give effect to the Protocol.

Real-Time Payments

Australian financial institutions, through the Australian Payments Clearing Association (APCA), are currently developing new "Real-Time Payments" infrastructure to enable players to make fast payments on low-value transactions (without the typical processing time of up to several days).

Under this proposal, new business architecture and ICT infrastructure will be developed for payments clearing amongst Australian deposit-taking institutions (ADIs) to offer real-time payment services to businesses and consumers. A clearing utility will connect all financial institutions to Reserve Bank of Australia (RBA) settlement facilities, enabling real-time transfers with the added feature of detailed purchase information to accompany the payment.[6]

Preliminary discussions have been held with APCA to explore opportunities for building a working relationship with the Protocol to encourage businesses to embrace innovative technology that supports prompt payment.

Establishing linkages between the Protocol and similar initiatives will help create synergies between the projects and support the overarching policy objective of on-time payments for business.

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[6] Further information about this initiative is available at the APCA website: http://www.apca.com.au/about-payments/future-of-payments/real-time-payments

Focus Questions

- Are there any other linkages that would complement the introduction of the Protocol?

Implementation Issues

The success of the Protocol in achieving a positive change in Australia's late payment culture will depend on its implementation design in order to ensure businesses are willing to sign up and gain real benefits. In particular, the aim is to improve payment behaviour without imposing additional regulatory burdens on business or place any unnecessary impediments that discourage participation.

There are a number of key implementation issues that will shape the operation of the Protocol including how businesses will participate; who will be responsible for administration and funding; issues regarding levels of compliance and complaints processes.

Feedback obtained during preliminary stakeholder consultations was wide-ranging on these issues and no clear implementation model was universally supported by business. However, it is clear that the model for the Protocol must strike the appropriate balance between allowing businesses to readily participate and ensuring a genuine commitment to prompt payment is maintained.

Administration

The operation of the Protocol will require an administrator with responsibilities for the provision and maintenance of the website and signatory list as well as the handling of the entry, compliance, reporting and complaints processes.

The administrator will also have an important role in continuing to build linkages with other payment initiatives and undertaking marketing activities to ensure momentum for the Protocol is maintained into the future.

Potential candidates for the administrator of the Protocol could include:

- peak industry associations;
- a professional financial association;
- a private sector firm with accounting or trade payment experience; or
- a Government agency.

Administration by a Government agency has the potential to leverage a wealth of program delivery experience and utilise existing customer service infrastructure to support the Protocol. However, stakeholders have pointed out that given its voluntary approach and dependence on widespread business support, it may be more appropriate for the Protocol to be industry-led. Preliminary feedback from business indicated a preference for a non-government third-party to administer the Protocol.

Government could work in partnership with business, potentially providing some initial seed funding, to help establish the foundations for the Protocol. Ownership of the Protocol could ultimately rest with industry once it has become firmly established. This approach has the advantage of allowing the Protocol to become an industry owned, funded and led voluntary scheme.

This approach is similar to the one adopted in the UK, where the Prompt Payment Code was initially set up by government but is now administered pro-bono by a not-for-profit credit management agency - the Institute of Credit Management (ICM). In addition to the Code, the ICM provides information and support, particularly for small businesses on cash flow issues.

An industry administrator of the scheme would need to be widely recognised as a neutral party to ensure support from a wide range of industry sectors. Issues in relation to the provision and storage of any confidential and potential conflicts of interest will need to be considered in developing the administration arrangements.

Focus Questions

- What type of entity should administer the Protocol? What are some of the advantages and disadvantages?
- What characteristics should be considered in selecting the most appropriate administrator?
- Which specific candidates should be further considered?
- Are there any other roles that the administrator should have?

Participation

A key issue in the design of the Protocol is the entry requirements for becoming accepted as a signatory to the Protocol. All businesses are eligible so long as they meet the suitable entry requirements. Overly onerous entry requirements may discourage business participation, while an entry threshold that is set too low may undermine the Protocol's credibility and integrity.

Referee Reports

In the UK, businesses gain entry to the Code by providing two referee reports from any of its suppliers to confirm that its current payment practices meet the requirements of the Code. The referee reports are provided to ICM, an independent third-party administrator, for consideration and acceptance. This is a relatively simple process that could be adopted for the Australian Protocol.

Incorporated into Company Charter

However, some concerns have been raised that providing two referee reports is not enough. Another option could involve businesses being required to incorporate the Protocol into their corporate charter or policy documents. This requirement would clearly demonstrate a commitment to the Protocol by its institutionalisation, but may involve some administrative costs and review of legal implications for businesses.

Variations of these options could be considered and balanced with any necessary ongoing compliance mechanisms (discussed further below) for maintaining the integrity of the Protocol.

Focus Questions

- What are the most appropriate entry requirements for the Protocol?
- Do the more onerous entry measures outweigh any administrative costs?

Compliance

Once a business has been accepted as a signatory to the Protocol, compliance measures may be necessary to ensure they continue to meet their payment commitment over time.

Compliance requirements for the Protocol could take several forms, including:

- no ongoing compliance checks, only ad hoc review on a complaints basis;
- requiring supplier referee reports to be renewed and updated annually;
- a process of random checks with small business suppliers in regard to payment practices and behaviours of signatories; and
- requiring signatories to submit a summary report of payment performance.

Stakeholders generally favour low compliance to minimise the burdens on business and encourage greater take-up of the Protocol. However, appropriate compliance measures can help build stronger public confidence in the Protocol and enhance its influence in the market.

Complaints based option

In the UK, compliance with the Code is tested based on complaints from suppliers that do not believe that a certain signatory is adhering to the Code. However, this facility is underutilised by suppliers in the UK and very few complaints, if any, have been made under the Code.

A modified approach could be considered for the Protocol in Australia. Affected suppliers could lodge a formal complaint with the administrator, specifying the conduct and circumstances of the breach of the Protocol. Where the administrator deems appropriate, they could act as an ‘honest broker’ and facilitate communication between the parties to have the matter resolved as quickly as possible.

If the issue is more complex or has a long running history, it may be more appropriate for the administrator to refer the matter for low-cost alternative dispute resolution (ADR) services available at the state or territory level.

Other compliance options

The other options outlined above impose varying degrees of compliance burdens on business and may be worth further consideration. A staged approach could also be considered whereby compliance requirements are only triggered in the event of a certain threshold being reached, for example, a significant volume of complaints being received against a signatory.

The objective is to ensure that businesses have confidence that the Protocol retains its meaningfulness for signatories long after the initial sign up period. The compliance options should be considered in light of the preferred entry requirement to ensure the Protocol operates effectively as a whole.

Focus Questions

- What is the most appropriate compliance approach for the Protocol?
- Should affected parties be able to lodge anonymous complaints? How could this be implemented to avoid frivolous and vexatious claims?
- How should complaints be handled to minimise adverse effects for the complainant while allowing fair opportunity for signatories to respond?

Consequences of non-compliance

It is envisaged that responsibility for dealing with non-compliance with the Protocol will rest with the administrator. The ultimate consequence of non-compliance will be the removal of the signatory from the Protocol and disallowance from use of the logo and branding entitlements. It is important to note that the Protocol is not intended to substitute debt recovery processes.

The issue to consider is the appropriate threshold that should be set to determine when removal of a signatory is warranted. It would be extremely difficult to formulate specific criteria that would lead to removal from the Protocol in a fair and reasonable manner.

It may be appropriate to outline a list of factors that an administrator may take into consideration, on a case-by-case basis, when making a decision to remove a signatory. For example:

- a widespread pattern of non-compliance supported by numerous complaints from different suppliers;
- lack of cooperation in resolving payment disputes;
- failure to attend any ADR processes;
- publishing or announcing corporate principles that directly contradict the Protocol; and
- breach of contract or competition laws that relate to payment terms.

The signatory should also be given the opportunity to respond to allegations and provide evidence before a decision for removal is made by the administrator. Businesses removed from the Protocol could be required to undergo a suspension period before they are able to reapply.

Focus Questions

- What compliance method should be adopted?
- Is the process for removal from the Protocol for non-compliance fair and effective?
- What must a company that has been removed from the Protocol show in order to reapply?

Communication

An effective communication strategy is vital for the success of the Protocol in raising awareness and support throughout the business community.

From the UK experience, the Minister for Small Business will be instrumental in raising the profile of the Protocol and raising support for it directly with the CEOs of the top 100 companies.

The proposed website and administrator will be responsible for disseminating information and promoting the Protocol. Assistance could also be sought from industry associations and accounting bodies that often deal closely with businesses, especially in relation to cash flow issues. It is envisaged that the Department will also leverage its broader business networks, for example, through AusIndustry and Enterprise Connect.

Focus Question

- What other communication channels could be used to drive awareness and support for the Protocol?

Other Issues

Alternative Regulatory Approach

The Protocol currently represents a voluntary, light-handed policy approach to encourage prompt payment between businesses. It relies on leveraging the commercial benefits of on-time payment to gain voluntary participation.

During initial stakeholder feedback, some concerns were raised that the Protocol does not go far enough to compel businesses, particularly the worst offenders, to pay on time. It has been suggested that a legislative approach may be needed.

In the UK, the *Late Payment of Commercial Debts (Interest) Act 1998*[7] was introduced prior to their voluntary Prompt Payment Code. Generally, the Act provides for automatic interest penalty charges to be applied for late payments in all business-to-business contracts.

However, the UK experience has shown that while these provisions are mandated by legislation, small businesses remain very reluctant to make use of them for fear of damaging their relationship, coupled with the cost of taking a debtor to court. Most supplier relationships are long standing and resorting to legal action is often not a practical option except as a final alternative.

[7] http://www.legislation.gov.uk/ukpga/1998/20/contents

On the other hand, the UK Code has demonstrated that a voluntary approach that gains the widespread support from influential players in large supply chains can have a positive effect on reducing payment times.

Australia has the opportunity to adopt a measured approach to foster a decisive shift in the late payment culture without introducing extra regulation. A successful and effective voluntary Protocol may avoid the need to explore other regulatory paths.

Focus Questions

- Should a legislative approach be considered in the Australian context?
- What are the advantages and disadvantages of such an approach?
- Will the introduction and operation of the Protocol help inform the need for any further policy response in this area?

Government Participation

Procurement

The Australian Government's procurement policy is to pay all small business invoices up to and including $5 million within 30 days of receiving a correctly rendered invoice. Small businesses can charge penalty interest if an invoice is not paid within 30 days for contracts worth up to $1 million. The Government recently released its 2011-12 Payment Performance Report. The Report shows almost 97 per cent of small business invoices were paid by the Government within 30 days.

Unfortunately, the Government's policy efforts to lead by example in paying its small business bills on-time seem to have had no discernible impact on improving private sector payment times.

Australian Government

It is intended that Departments and agencies at all tiers of government will be able to become signatories to the Protocol. Some stakeholders have suggested that the Government could do more to encourage adoption of the Protocol by referencing it within Government procurement practices. Specifically, Government could consider taking the view that being a signatory

to the Protocol should be a relevant factor for consideration during the tendering process for awarding Government contracts. Some stakeholders indicated that this concept should go further – to make it a compulsory requirement for businesses seeking Government procurement contracts to become signatories to the Protocol.

It should be noted that this concept would require significant whole-of-government consultation to ensure it aligns with Government procurement policy.

State, Territory and Local governments

Particular emphasis has been placed on the participation of state, territory and local governments that undertake the lion's share of small business procurement. State, territory and local governments regularly engage small business suppliers in their local community on a variety of goods and services, from playground construction to office cleaning services. Their support of the Protocol will help generate further critical mass for its widespread adoption across the business community.

While some may argue that the payment practices amongst other tiers of government already adhere to the Protocol, a consistent and harmonised approach would give businesses greater certainty in their dealings across government.

Further consultation with state and territory governments and local government associations will be necessary to identify opportunities for supporting the Protocol.

Focus Questions

- How should all tiers of Government support the Protocol?
- How important is it for state and territory and local government to participate in the Protocol?

Summary of Key Focus Questions

Culture of late payments

- What are the main causes of late payments, and how do they differ in various industries?

Prompt Payment Protocol

- What are the fundamental principles that should be included in the Protocol?

Administration

- What type of entity is best placed to administer the Protocol?

Participation

- What requirements should be met to gain entry to the Protocol?

Compliance

- What is the most appropriate compliance approach?

Government Participation

- How should governments participate in the Protocol?