



European Bank
for Reconstruction and Development

Factoring, reverse factoring and other tools for access to finance

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Outline of presentation

1. Problem of late payments
2. Factoring – good mitigation tool
 - Defining factoring
 - Types of factoring
 - Benefits of factoring
 - Misuses of factoring
3. Regulatory framework
4. Legislative framework
5. EBRD work on promotion of factoring

- Turkey – Financial Leasing, Factoring and Financing Companies Law 2012
- Serbia – Factoring Law 2013
- Croatia – Factoring law under preparation
- Montenegro – looking into regulating

**Squeezed liquidity of buyers and suppliers
caused by late payment culture and hardened access to credit
(World Economic Forum*)**

*<http://reports.weforum.org/financial-development-report-2012>

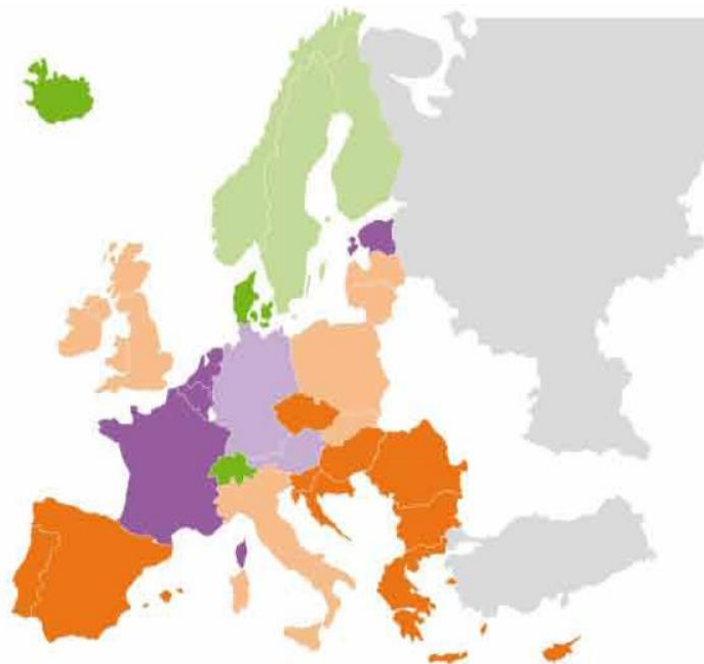
LATE PAYMENTS – Liquidity issues

European Payment Index 2013 (Intrum Justitia Group, <http://www.intrum.com/uk/>)

	Payments between 30 – 90 days	Payments over 90 days	Businesses adversely affected by late payments
Bulgaria	28%	24%	73%
Croatia	40%	29%	73%
Latvia	25%	25%	64%
Lithuania	33%	16%	93%
Poland	37%	8%	60%
Romania	29%	25%	87%
Russia	35%	7%	73%
Slovenia	26%	18%	86%
Turkey	43%	37%	86%

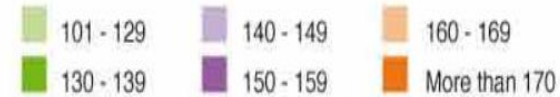
LATE PAYMENTS – Liquidity issues

European Payment Index 2013



2013

Legend



Risk Index Explanation of the Payment Index values

100	No payment risk, cash on delivery, pre-payment, no credit
101-129	Low risk profile, stay alert to keep this profile
130-139	Low to medium risk profile, intervention necessary, take action now
140-149	Medium risk profile, action needs to be taken
150-159	Medium to high risk profile, take immediate actions to lower the risk
160-169	High risk profile, immediate actions are necessary
More than 170	Emergency risk profile

PUBLIC MEASURE AGAINST LATE PAYMENTS

- EU Directive 2011/7/EU on combating late payment in commercial transactions
 - Had to be transposed by 16 March 2013
 - Public authorities to pay for goods and services within 30 calendar days
 - Private sector should pay their invoices within 60 calendar days
 - Penalty interest of 8% above base rate chargeable
- Serbia – 2012 Late Payment Law
 - Public authorities to pay for goods and services within 45 calendar days
 - Private sector should pay their invoices within 60 calendar days
 - Penalty interest chargeable, additional fines possible
- Turkey –2012 Commercial Code (Article 1530)
 - Addresses only private sector
 - Payment of invoices to be made within 30 - 60 calendar days
 - Penalty interest of 8% above base rate chargeable, additional fines possible

BUSINESSES RESPONSE

Negative

- Delay account payable
- Reduce inventory
- Increase prices
- Negotiate longer payment terms

Unlikely

- Bank lending
- Increase working capital
- (Cut overhead)

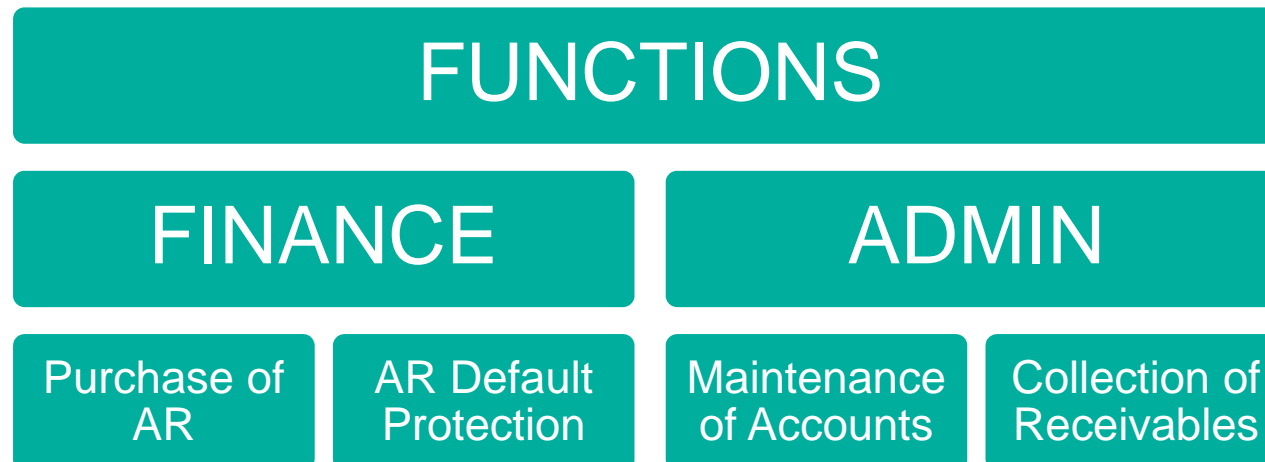
Positive

- Actively pursue accounts receivables
- Bill clients faster
- Sell invoices

All three positive actions found in factoring

FACTORING FUNCTIONS

1988 UNIDROIT Convention on International Factoring



TYPES OF FACTORING

Three basic criteria

Transfer of risk	Place of business	Debtor notification
<ul style="list-style-type: none">• Non-recourse• Recourse	<ul style="list-style-type: none">• Domestic• International (one or two factor system)	<ul style="list-style-type: none">• Disclosed• Silent (Invoice discounting)

Other categorisations possible - depending on:

- the client's involvement in collection (client as agent for factor)
- due date for payment of purchase price (maturity or payment of invoice)
- AR debtor contracts with factor instead of creditor - Reverse Factoring (Confirming, Supply Chain Finance)

BENEFITS OF FACTORING

SME SUPPLIERS

- Quick access to working capital
- Financing against buyers' credit standing
- Cuts administration overhead costs
- Off balance sheet finance (non-recourse)
- Supports growth and diversification of business

BUYERS

- Extend payment terms
- Outsourced ledgering (reverse factoring)
- Improved relationship with suppliers

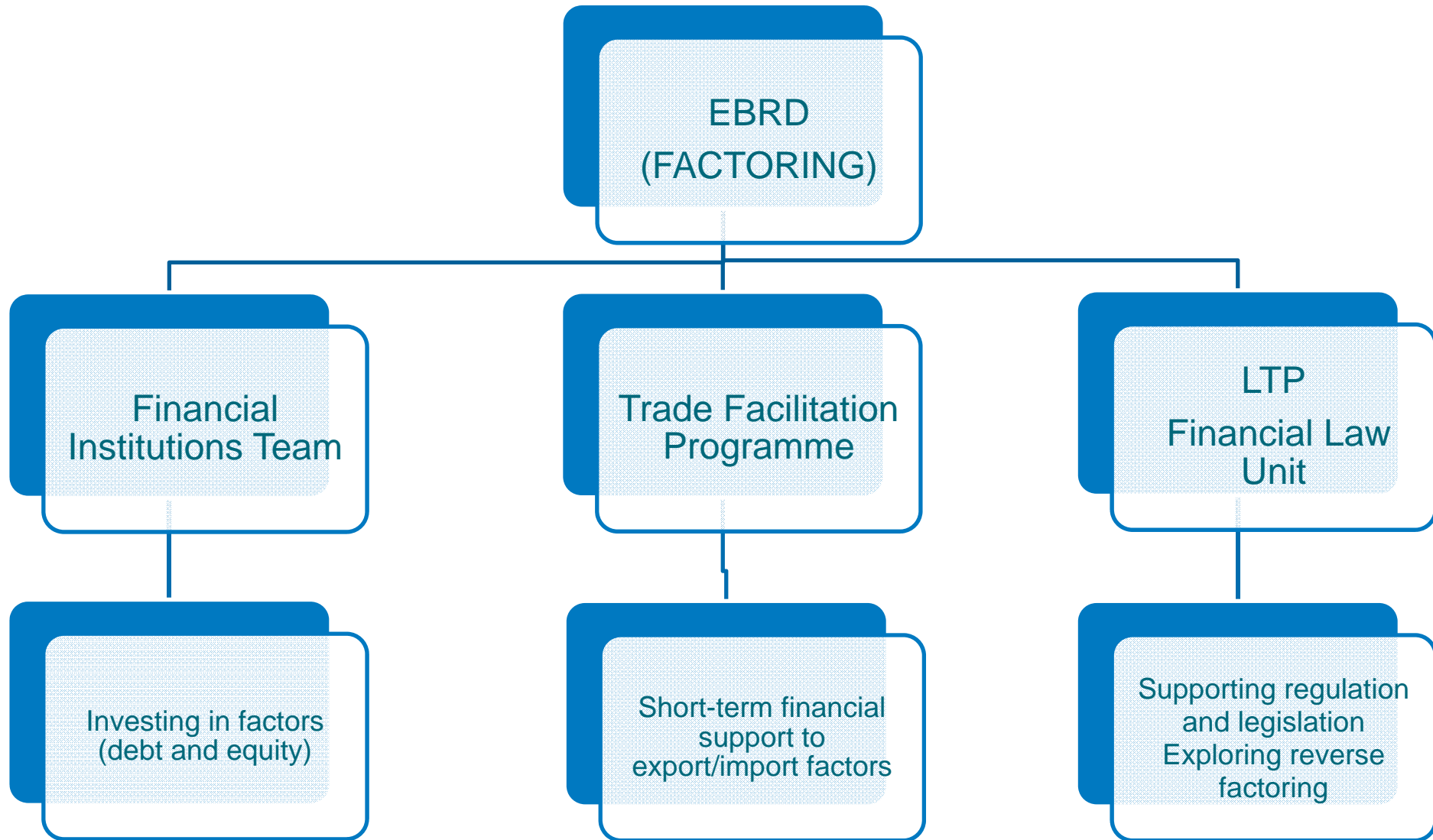
ECONOMY

- Transfers credit risk from real to financial sector (non-recourse)
- Supports growth of businesses

MISUSE OF FACTORING

Improper use	
For capital expenditures - equipment financing	Transforms working capital into long term assets – (squeezes liquidity down the road)
Last resort financing for loss making business	Limited breathing space as long as new receivables are created (danger of recourse) – overtrading

EBRD AND FACTORING



REGULATING FACTORING COMPANIES

Three approaches

Not regulated

- UK – ABFA
Russia, Slovakia,
Belgium,
Netherlands,
Poland, Czech R.,
Lithuania, Estonia

Regulated - no capital adequacy

- Germany – BaFin
Portugal,
Romania,
Bulgaria, Serbia,
Norway, Turkey,
Croatia, Greece,
Hungary, Malta

Regulated with capital adequacy

- Italy, France,
Austria, Spain

licence, start up capital, qualified holdings control, approval of management, reporting, audit, internal organisational requirements (risk management and outsourcing)

Basel capital adequacy requirements with some relaxations based on source of factor's funding or on factor's membership in a group

REGULATING FACTORING COMPANIES

Three traditional criteria for application of capital adequacy regime

large source of credit (macroeconomic significance)	deposit taking	intermediary in payment systems
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FSB, ECB and EU on shadow banking

- EU Green Paper 2012 - Broad definition raised concerns (credit intermediation and risk transfer component in particular)
- EC Communication on Shadow Banking – 04.09.2013 (securitisation vehicles, money market funds, hedge funds, PE funds, credit guarantees) – no factoring.



BENEFITS OF LIGHT REGULATION

licence, start up capital, qualified holdings control, approval of management, reporting, audit, internal organisational requirements (risk management and outsourcing)

Legitimises the industry	Separates factoring from shadow banking, bad banks (NPLs)	Incentivises review of legislative base (pragmatic approach)	Might help attract investments
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Factoring Based On Assignment of Accounts Receivable Important issues

- Sale or security (non recourse - recourse)
- Assigning future receivables (identification, bundle notice)
- Priority rules (pledge, extended ROT)
- Necessary formalities (availability of electronic assignment)
- Effects of prohibition on assignment clauses

SHOULD THE PROHIBITION ON ASSIGNMENT CLAUSE BE RENDERED INEFFECTIVE AGAINST FACTORS?

Two possible effects of the clause:

1. To render the assignment invalid
2. To allow debtor to disregard notice

Arguments in favour

- Abuse of market position
- Know your creditor not relevant for trade credit (short term fixed relationship)
- Factoring regulated service
- Impedes competition for trade credit
- Impedes factoring (impossible or risky)
- Competition policy takes time

Arguments against

- Freedom of the contract
- Administrative burden – costs
- Choose your creditor (financiers – less flexible)
- Competition Law Issue

CLAUSE RENDERED INEFFECTIVE

INEFFECTIVE FOR FACTORING

NATIONAL LAWS

- **US** (UCC9)
- **Canada, AU** (PPSA)
- **Italy** (Factoring Law)
- **Serbia** (Factoring Law)
- **Latvia** (Comm. Code)
- **Romania** (Law 99/1999)
- **Croatia** (Draft Law)
- **Greece** (practice)
- **France** (CC Subrogation)
- **Austria** (CC - limited)

INTERNATIONAL CONVENTIONS

- Unidroit Convention on International Factoring (1988), Art 6
- UN Convention on the Assignment of Receivables in International Trade (2001), Art 9

Basic elements

Platform

Agreements

Supply
Chains

Financing
Chains

Automatic
offers

Operator
Electronic transfers

Buyers
Factors
Suppliers

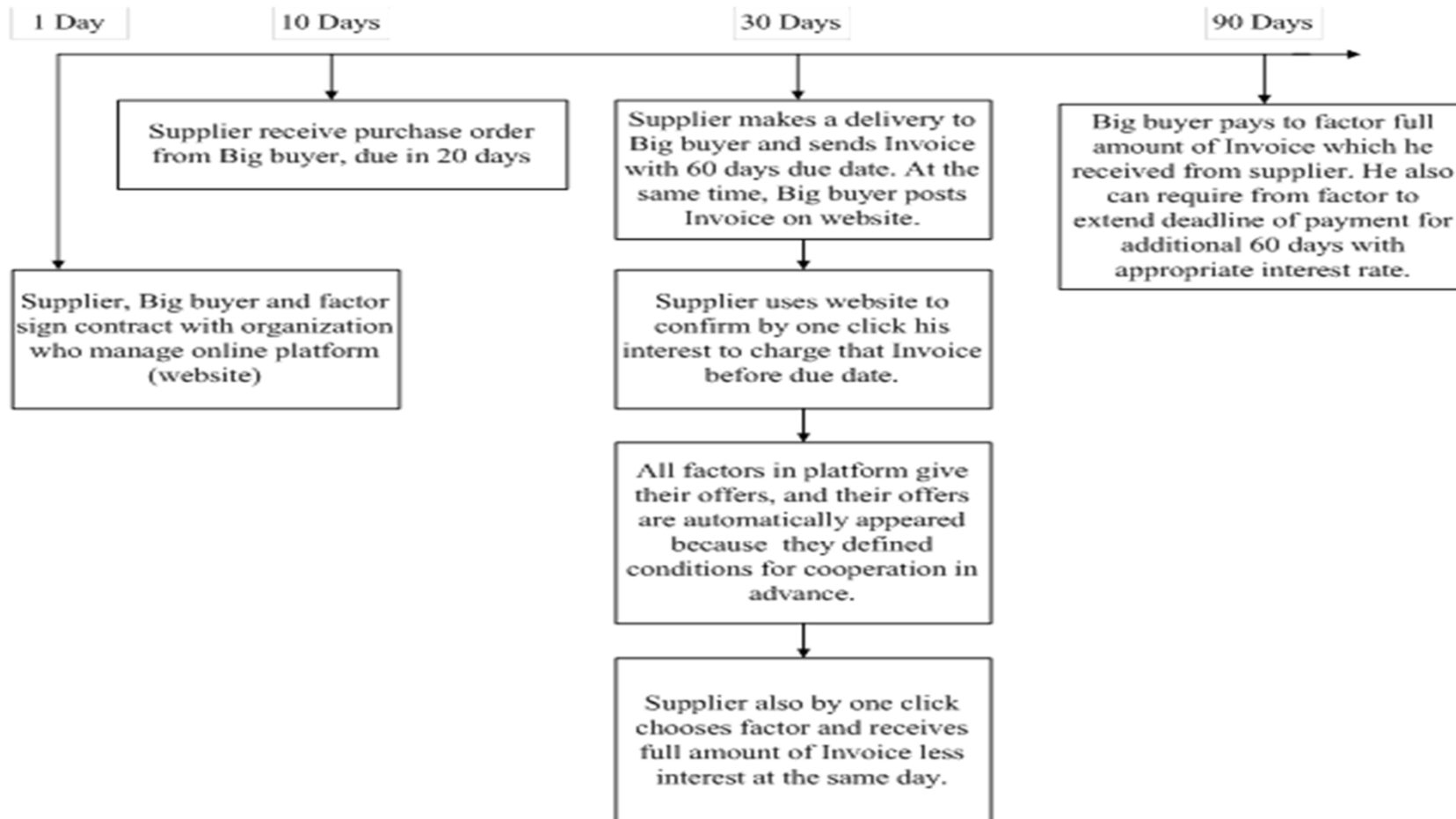
Suppliers grouped
under big buyers

Interested factors
grouped under big
buyers
(competition)

Offers created
upon electronic
confirmation of
invoice under - pre
generated terms

REVERSE FACTORING PLATFORM

Typical transaction



Developing Reverse Factoring - Challenges

Factors do not want competition

Include state owned buyers (companies, funds, etc.) on the platform to attract factors

Channel SME support financing via platform (state, IFI, etc. - risk sharing, participations, subsidies, etc.)

Buyers want to do it themselves (earning margin)

Make prohibition on assignments ineffective

Promote benefits of platform

Example of Reverse Factoring Platform

- Nafin - Mexico's development bank started platform in 2001
- Factoring market share from 2% in 2001 to 75 % in 2010
- In 2009 - 700 big buyers (35 % public and 65 % private sector)
- In 2009 - 27,000 SMEs funded, amounting to US\$15.9b
- Nafin generates revenues out of the interest that factors pay for their capital refinancing (subsidy – development bank)
- Out of revenues it covers all legal expenses and factoring fees
- Factors only charge interest
- Nafin is profitable and there are thoughts on state (subsidy) exit.

OTHER TOOLS FOR ACCESS TO FINANCE

Apart from factoring Financial Law Unit promotes

Secured transactions (modernisation)	Credit information systems (efficiency increase)	Grain warehouse receipts (systematization)	Crop receipts (introduction)
<p>Flexible laws conducive to modern business transactions</p> <p>Electronic security interests registries</p>	<p>Wide range of credit information collected (trade credit, utilities)</p> <p>Wide Accessibility</p> <p>Transparent procedures</p>	<p>Increasing reliability (licencing, indemnity funds)</p> <p>Post harvest collateral</p> <p>Trading</p>	<p>Pre-harvest financing</p> <p>Future output as collateral</p> <p>Monitoring and Priorities</p> <p>Efficient enforcement</p>