Title: Measure to nullify ban on assignment clauses in a debtors terms of sale. **IA No:** **Lead department or agency:** Department for Business, Innovation and Skills **Other departments or agencies:**	Impact Assessment (IA) **Date:** 17/10/2014 **Stage:** Consultation **Source of intervention:** Domestic **Type of measure:** Secondary Legislation **Contact for enquiries:** Charmaine Phillips E: charmaine.phillips@bis.gsi.gov.uk Tel: 0207 215 2733
Summary: Intervention and Options	**RPC Opinion:** RPC Opinion Status

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, Two-Out?**	**Measure qualifies as**
£9.0m	£9.0m	-£0.8m	Yes	Zero Net Cost

What is the problem under consideration? Why is government intervention necessary?

Bans on assignment of trade receivables prohibit the supplier from selling the debt from an accounts receivable, typically from an invoice, onto a third party financer. We believe these bans are relatively commonplace in contracts yet serve no benefit to effective market functioning. A ban on assignment clauses in a debtors' terms of sale tend to be in place because of historic and unrevised contractual arrangements.

Government intervention is necessary to pass legislation prohibiting such bans, in order to remove these contractual barriers and allow business, especially small to medium size businesses, the freedoms and flexibilities to make best use of invoice financing in a way that benefits them. This measure will seek to nullify the ban on assignment, meaning that businesses will not need to retrospectively revise their contracts.

What are the policy objectives and the intended effects?

The aim of this policy will be to remove a contractual barrier to invoice financing and improve the accessibility for businesses to gain this type of finance. This will help businesses lacking the sorts of assets that serve as collateral for a bank loan to access invoice financing.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Option 0: Do nothing
Option 1: Override bans on the assignment of trade receivables for goods and services (preferred option)
Option 2: provide that terms are ineffective in relation to certain parties
Option 3: provide that such terms are effective only in relation to certain persons for certain purposes

Will the policy be reviewed? It **will** be reviewed. **If applicable, set review date:** March/2020

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** **Yes**	**< 20** **Yes**	**Small** **Yes**	**Medium** **Yes**	**Large** **Yes**
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** **N/A**	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible SELECT SIGNATORY: .... Date: ....

Summary: Analysis & Evidence

Policy Option 1

Description: Override bans on the assignment of trade receivables for goods and services (preferred option)

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year 2014	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 3.6	**High:** 14.7	**Best Estimate:** 9.0

COSTS (£m)	**Total Transition** (Constant Price)	Yea	**Average Annual** (excl. Transition) (Constant	**Total Cost** (Present Value)
Low	0.0		0.0	**0.0**
High	0.0	1	0.0	**0.0**
Best Estimate	0.0		0.0	**0.0**

Description and scale of key monetised costs by 'main affected groups'

The only costs will be familiarisation costs. It is the invoice financiers, rather than the businesses holding the restrictive contracts, that are aware of these clauses. Hence our estimate of the familiarisation costs falls solely upon a best estimate of 47 invoice financiers, and the best estimate of familiarisation costs is just under £850 across all invoice financers. We have assumed that there will be no cost of nullifying the ban on assignment clause(s) in existing contracts as terms will remain in debtors' contracts. There will be no ongoing costs. Nulification would mean that contracts cotinuning to apply such restrictions would not need to be revised.

Other key non-monetised costs by 'main affected groups' N/A

N/A

BENEFITS (£m)	**Total Transition** (Constant Price)Years		**Average Annual** (excl. Transition) (Constant	**Total Benefit** (Present Value)
Low	0		0.4	**3.6**
High	0	0	1.7	**14.7**
Best Estimate	0		1.0	**9.0**

Description and scale of key monetised benefits by 'main affected groups'

Benefits will arise because invoice financers will no longer incur the administration costs of waivers and workarounds which some seek when they come across a ban on assignment clause. To monetise the benefit we estimate how many waivers/workarounds there are in a year and how much they cost. We estimate these benefits by far exceed the costs, and are at around £9m.

Other key non-monetised benefits by 'main affected groups'

Our survey to the Asset Based Finance Association (ABFA) members highlighted a number of other benefits which we have not been able to monetise. Results show that some invoice financiers may refuse to offer any finance or reduce available funding in the presence of a Ban on assignment. They may also increase lending rates to reflect additional risk and require additional security due to the presence of ban on assignment. With nullification we anticipate fewer straight refusals and reduced funding, lower rates and less security required for invoice finance.

Key assumptions/sensitivities/risks — **Discount rate** 3.5

Both costs and benefits are informed by a self-selected survey aimed at members of ABFA conducted for the IA. The total number of invoice financers in the market is unknown, we have a best estimate of 47 with a range of 31-54,Monetised costs and benefits include assumptions on hours and seniority of employee that individual tasks require. We have assumed the number of waivers and workarounds sought annually does not significantly differ each year. We have assumed that a majority of ban on assignment clauses are unintentionally in a debtor's terms of sale.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			**In scope of**	**Measure qualifies**
Costs: 0.0	**Benefits: 0.8**	**Net:0.8**	Yes	Zero net cost

Summary: Analysis & Evidence

Policy Option 2

Description: (b) to provide that such terms are ineffective in relation to certain parties, for example to provide that they do not stop an invoice financier benefitting from the assignment;

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year 2014	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -	High:-	Best Estimate: -

COSTS (£m)	Total Transition (Constant Price) Yea		Average Annual (excl. Transition) (Constant	Total Cost (Present Value)
Low	-	-	-	-
High	-		-	-
Best Estimate	-		-	-

Description and scale of key monetised costs by 'main affected groups'

No costs have been monetised at this stage

Other key non-monetised costs by 'main affected groups'

Under this option we again assume that there will be no nullification costs as no contracts will need to be retrospectively changed. However, due to the complexities around when a ban on assignments is valid, we assume that more parties will need to become familiar with this policy. We also assume under this option there will be ongoing costs as suppliers would need to identify invoice financers and institutions who wish to lend finance on the basis of invoices as collateral will need to know if they are classed as an invoice financer under the policy.

BENEFITS (£m)	Total Transition (Constant Price) Yea		Average Annual (excl. Transition) (Constant	Total Benefit (Present Value)
Low	-	-	-	-
High	-		-	-
Best Estimate	-		-	-

Description and scale of key monetised benefits by 'main affected groups'

Not monetised any benefits at this stage

Other key non-monetised benefits by 'main affected groups'

Dependent on who would be classed as an invoice financer under the policy, the benefits maybe equal to our preferred option for example in the case that all 47 (best estimate) firms that we estimated may provide invoice financing currently are classed as an invoice financer. If only a selection are deemed invoice financers under the terms of the policy the benefits are reduced as those not captured are the invoice financing definition may still need to seek waivers and work arounds in the presence of a ban on assignment clause.

Key assumptions/sensitivities/risks **Discount rate (%)** 3.5

More people will need to become familiarised with this policy and there would be ongoing costs of identified who is and is not an invoice financer.

While we have not been able to quantify the benefits we believe it is reasonable to assume that these will be higher than option zero, but no greater than option one and three.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			In scope of	Measure qualifies
Costs: 0.0	**Benefits: 0.0**	**Net:0.0**	Yes	-

Summary: Analysis & Evidence

Policy Option 3

Description: to provide that such terms are effective only in relation to certain persons for certain purposes, e.g. providing that damages are payable for assigning in breach of a term, without affecting the validity of the assignment or the interests of the assignee

FULL ECONOMIC ASSESSMENT

Price Base Year 2013	PV Base Year 2014	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -	High:-	Best Estimate: -

COSTS (£m)	Total Transition (Constant Price)	Yea	Average Annual (excl. Transition) (Constant	Total Cost (Present Value)
Low	-	1	-	**-**
High	-		-	**-**
Best Estimate	-		-	**-**

Description and scale of key monetised costs by 'main affected groups'

No costs have been monetised at this stage

Other key non-monetised costs by 'main affected groups'

Under this option we again assume that there will be no nullification costs as contracts will not need to be retrospectively changed. However, due to the complexities around the ability of a party to sue when damages are incurred due to an assignment, we assume that more parties will need to become familiar with this policy thereby leading to larger costs. Businesses will also bear familiarisation costs associated with understanding terms where assignment has disadvantaged them which could surmount to considerable legal costs.

For those firms who were previously able to include ban on assignment clauses for the purpose of commercial protection, this policy may lead to additional costs if they now need to sue for damages.

BENEFITS (£m)	Total Transition (Constant Price)	Yea	Average Annual (excl. Transition) (Constant	Total Benefit (Present Value)
Low	0	0	0.4	**3.6**
High	0		1.7	**14.7**
Best Estimate	0		1.0	**9.00**

Description and scale of key monetised benefits by 'main affected groups'

Not As the ban on assignment clause will be nullified as in option one, we believe that the benefits to this option will be the same as the first option.

Other key non-monetised benefits by 'main affected groups'

Our survey to the Asset Based Finance Association (ABFA) members highlighted a number of other benefits which we have not been able to monetise. Results show that some invoice financiers may refuse to offer any finance or reduce available funding in the presence of a Ban on assignment. They may also increase lending rates to reflect additional risk and require additional security due to the presence of ban on assignment. With nullification we anticipate fewer straight refusals and reduced funding, lower rates and less security required for invoice finance.

Key assumptions/sensitivities/risks **Discount rate (%)** 0.0

As the ban on assignment clause will be nullified as in option one, we believe that the benefits to this option will be the same as the first option. While we have not been able to quantify the costs we believe it is reasonable to assume that these will be higher than option one and two and option zero. We have assumed that a majority of ban on assignment clauses are unintentionally in a debtor's terms of sale.

BUSINESS ASSESSMENT (Option 3)

Direct impact on business (Equivalent Annual) £m:			In scope of	Measure qualifies as
Costs: 0.0	**Benefits: 0.0**	**Net:0.0**	Yes	-

Background

Problem under Consideration

1. All businesses are highly dependent on cash flow and often require access to alternative (external) sources of finance in order to invest and grow. A barrier to accessing this finance is a lack of significant collateral in order to offset lending risks for financers. This is a particular issue for small and medium sized businesses.

2. Traditionally, bank debt, whether through a loan or overdraft, has been the primary source of external finance for businesses to manage cash flow. However, the volume of lending to businesses has fallen from a 2008 peak of approximately £720 billion to approximately £450 billion in 2014.[1]

3. Given this retraction in traditional bank lending, it has become increasingly important for businesses to access alternative forms of finance. However, many small and medium sized businesses may not use the full range of options available for managing cash flow as a normal part of doing business. In addition, there are barriers to accessing some alternative forms of finance. A potential contractual barrier is a ban on the assignment of trade receivables.

4. For larger businesses, there are greater opportunities to access alternative finance. Invoice financing provides an option in particular to small and medium businesses in a market where options on types of lending can be narrow.

5. For many businesses, a major part of their assets will be in the form of money owed to them for goods and services (accounts receivables). The supplier can raise money on the strength of their receivables (monies owed to the supplier by the debtor) by taking a loan which is secured by a charge over the receivables. Alternatively, they can sell their receivables outright to a third party finance provider – an assignee. These forms of financing are collectively referred to as invoice financing.

6. Therefore invoice financing allows businesses to access working capital against the security of monies owed to them. This financial product is especially useful as a means of cash flow management to businesses that provide goods and services under a contract, or businesses that need to raise additional finance but lack fixed assets to provide security to obtain a loan.

7. Bans on assignment of trade receivables refers to a clause in a debtor's terms of sale which prohibits the supplier from selling the debt from an accounts receivable, typically from an invoice, onto a third party financer. In some cases, the presence of a 'ban on assignment' clause can be the deciding factor in businesses being declined for invoice finance.

[1] BIS calculations, based on BBA, Bank of England, ONS and BIS data

8. There is a distinction between invoice financers that offer factoring and invoice discounting. An invoice financer offering factoring will take on the supplier's sales ledger and negotiate with the debtor for payment. In cases where a ban on assignment for trade receivables clause is present in a contract, the factor will typically ask for a waiver of the ban on assignment. For invoice discounters, the work around is common practice, because the supplier will keep responsibility for its sales ledger maintenance and will carry on negotiating with the debtor. This practice means that the debtor is not necessarily informed about the assignment of the trade receivable. These practices are explained further in Annex A.

9. It is not possible to provide an exact figure for the prevalence of bans on assignment in business contracts. However, our survey of ABFA members found that a) 100% of those respondents who said they offer factoring services have come across ban on assignment clauses and b) 93% of respondents who said they offer invoice discounting have come across ban on assignment clauses.

10. A non-representative online survey aimed at large firms was conducted as part of the wider prompt payment policy development survey which contained some questions relating to ban on assignment. The survey received 35 valid responses. When respondents were asked 'Do you include a 'ban on assignment' clause in your contracts that prevents the assignment of invoices to third parties?' 30% of the 33 responses said yes with a further 21% saying they do not know. The survey then asked those respondents who said yes 'Approximately what proportion of contracts does the 'ban on assignment' apply to?' 56% of the 9 responses said 96% to100%.There was one response for each of the following categories: 26% to 50%, 51% to 75%, 76% to 95% and "Don't know".

11. Furthermore, discussions with invoice financers suggests that bans on assignment are very common in business contracts across most sectors and are especially common in contracts issued by larger businesses. This anecdotal evidence has been borne out by separate conversations that we have had with a number of large retailers, construction firms and manufacturing businesses which have confirmed that their standard commercial contract will contain a ban on assignment which extend to the assignment of trade receivables.

12. This can impact negatively on the ability of small and medium sized businesses to invest and grow, and can have further serious consequences on cash flow, potentially leading to a firm declaring bankruptcy.

Barrier to Finance: Ban on Assignment

13. We understand that in many cases a ban on the assignment of trade receivables is an unintended consequence of a wider ban on assignment within the contract, often designed to prevent sub-contracting. Businesses will often have a ban on assignment clauses as part of historic and unrevised contractual arrangements, rather than intentionally including them. We plan to consult our stakeholders on this very point and test whether this is the case in the majority of contracts containing ban on assignment clauses. We expect that nullifying ban on

assignment clauses for trade receivables will not impact on other assignment bans and therefore not impose additional costs to debtors or suppliers.

14. We recognise that there can be some potentially legitimate reasons for a business to seek to ban the assignment of trade receivables. These include exercise of a right to set off and retention of commercial confidentiality. Set off allows a debtor to consolidate invoices from multiple transactions, including debts the supplier owes to the debtor, into a single invoice. Assignment makes this arrangement more difficult because the ability to consolidate multiple invoices becomes difficult with the introduction of a third party who may have an interest in an invoice which makes up the final payment. Commercial confidentiality can be important to some debtors who may wish to remain anonymous in a transaction. The disclosure of the debtor to the invoice financer compromises that confidentiality. Respondents to our discussion paper, “Building a Responsible Payment Culture”, thought that these benefits did not outweigh the merits of nullifying such bans.

15. A ban on assignments restricts invoice financing as an option to accessing finance. When an invoice financer is considering advancing money to a client against the value of their trade receivables, the financer will primarily base their decision regarding the terms of any advances on the ability of the client to repay monies advanced by the financer. A ban on assignment can particularly increase the risk of providing invoice finance to businesses. This is because:

    a) The debtor may terminate the contract and refuse to pay monies owed to the supplier/client on the grounds of breach of contract; and/or

    b) In the case of the supplier/client becoming insolvent, the debtor may refuse to pay their trade debts already owed under contract with the suppler/client on the grounds that the contract was invalidated by the assignment, or on the grounds that due to the ban on assignment, they do not recognise the security interest of the third party financer. In cases of equitable assignment, the financer does not legally have the right to pursue the debt owed in their own name and so must rely on the administrator of the insolvent client to pursue debts, which it may not do successfully.

16. This increased risk impacts in differing ways on the provision of finance, often depending on a variety of factors including the operating model and risk appetite of the financer, the financer’s relationship with the client, the reputation and credit history of the debtor, etc. These include:

    a) The finance provider may outright decline to offer any invoice financing to the client. This can often occur when the loan book of the client is highly concentrated and the invoices in question are subject to bans on assignment. Some invoice finance trading platforms may also decline to offer any financing to the client/supplier submitting an invoice for trading which is subject to a ban on assignment.

b) When the existence of a ban on assignment is known, it will almost invariably necessitate resource expenditure (time and expertise) on the part of the invoice financer and/or client to remove the ban on assignment or mitigate against the increased risk to repayment. The finance provider may seek a waiver of the ban from the debtor which removes the obstacle of the ban. But if a waiver from the debtor is not obtainable, it may be necessary to establish a 'work-round', which reduces the risks faced by the financers. This might typically involve obliging the client to set up a separate trust account into which they must require monies owed from the debtor to be paid, and/or establishing a power of attorney to pursue monies owed in trade debt to the client in the case of insolvency. These 'work- rounds' are necessitated by the existence of the ban on assignment and can result in additional costs that may be borne by the client either directly or through the pricing of the financing eventually obtained. We have sought to distinguish between waivers and work-around measures in our costs section.

c) Bans on assignment may also result in a reduction in the amount of financing available to the client, and at the same time increase the cost of the financing that is offered to them by the invoice financer. If a financer is concerned that a number of invoices on the loan book of the client may be subject to contractual bans on assignment, the financer may decide to advance finance against only a reduced percentage of the value of the invoices, or against a reduced number (volume) of invoices on the loan book. As traditional 'whole loan book' invoice financing is priced both by the discount rate against the financing used by the client and a fixed service fee (either fixed quantum or fixed % of turnover), the cost of financing is therefore increased as the 'value for money' of the service fee is reduced.

International Comparisons and Precedents

17. There is international precedent for nullifying the ban on assignments. In May 1988, UNIDROIT (L'Institut International pour L'unification du Droit Privé) adopted a Convention on International Factoring, which stated that "the assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment" (Article 6, 1). In 2001, UNCITRAL (the United Nations Commission on International Trade Law) adopted the Convention on the Assignment of Receivables in International Trade which states that "an assignment of a receivable is effective notwithstanding any agreement between the initial or any subsequent assignor and the debtor or any subsequent assignee limiting in any way the assignor's right to assign its receivables" (Article 9, 1).

18. Other advanced economies have introduced legislation to nullify bans on the assignment of trade receivables directly, or have created a legislative framework for the registration of property securities that effectively allows for the

assignment of trade receivables irrespective of contractual bans to that effect. These include the US, Australia and Canada,

19. Under the US Uniform Commercial Code (Article 9-406), ban on assignments clauses and the requirement for the debtor's consent for assignment is invalidated. However, the debtor should receive notification that the payment has been assigned to a financer.

20. In Australia, the Personal Property Securities Act 2009 nullifies ban on assignment clauses. There is also a provision to allow the debtor to sue for damages that could be incurred by the assignment between the financer and the supplier. The full effects of the Act are currently being reviewed by the Australian Government, with a final report due in January 2015. We aim to analyse the results of this report for our final Impact Assessment.

21. In Canada each state has adopted a Personal Property Security Act. The Ontario version of the Act nullifies a ban on assignment and contains a provision which entitles the debtor to compensation if an assignment causes damages to it.

Previous attempts to tackle the problem in the UK

22. On 31 August 2005 the Law Commission published a set of recommendations (LAW COM No 296) on reforming the registration of company security interests. This included a recommendation to 'override' bans on the assignment of trade receivables. The report stated that "in a contract between a company and a third party creating a receivable payable to the company, a term that purports to prohibit or restrict assignment of the account should be of no effect against a third-party assignee" (LAW COM No 296, 2005, Para 6.73, p.155).

23. In 2008, both the Scottish and UK Governments changed their policies to recommend against the use of bans on the assignment of receivables by public sector authorities. On 16 June 2008, the Office of Government Commerce (Efficiency and Reform Group, Cabinet Office) issued a Procurement Policy Note instructing recipients "to permit explicitly, the assignation of debts arising under a contract". As with all OGC model terms, this change in policy was aimed at Contract Authorities in Central Civil Government, with Contracting Authorities in the Wider Public Sector encouraged to adopt the OGC model contractual terms. However, from discussions with invoice financers and surveys we have carried out it is apparent that bans on assignment of trade receivables have continued to be used in UK business contracts, including in public sector supply chains.

24. In April 2013, the Companies Act 2006 (Amendment of Part 25) Regulations 2013 came into force. The Regulations amended the Companies Act 2006 relating to company security interests. However, the Regulations only implemented some of the Law Commission's recommendations. Due to this partial implementation some recommendations, including the recommendation to make ineffective contractual bans on assignment, were not implemented at this time.

25. In December 2013, the Department for Business, Innovation & Skills published a Discussion Paper entitled 'Building a Responsible Payment Culture'. The Discussion Paper asked "would removing contractual barriers to selling invoices (e.g. as a result of a ban on assignment) be helpful to small and medium sized businesses by increasing their access to services such as factoring and invoice finance?"; about half of the respondents agreed that removing ban on assignment clauses would be helpful.[2] The majority of respondents who disagreed suggested that the cost of waivers and workarounds would dissuade small businesses from accessing invoice financing; however, we anticipate that the nullification will make access to finance easier.

26. In May 2014, the Department for Business Innovation & Skills published a response to the 'Building a Responsible Payment Culture' Discussion Paper. The Government Response stated the intention "to introduce legislation to tackle contractual barriers such as bans on assignment when Parliamentary time permits".

27. In June 2014, The Government introduced the Small Business, Enterprise and Employment Bill into Parliament. This Bill includes two clauses relating to the nullification of bans on the assignment of trade receivables. The first clause provides an enabling power for the Secretary of State to introduce regulations to nullify bans on the assignment of trade receivables, and the second introduces an exemption for financial services and products.

28. Over the summer we undertook a programme of informal consultations with businesses, financers and legal experts. We conducted a non-representative survey aimed at large firms as well as a separate survey of invoice financers who were members of Asset Based Finance Association (ABFA). We intend to launch a formal consultation on the details of the secondary legislation shortly.

Rationale for intervention

29. Bank lending to small and medium sized businesses has fallen since the financial crisis and a major obstacle to lending is based on affordability. Typically, a business would use their accounts receivable as collateral for invoice financing, but a ban on assignments restricts the possibility of accessing finance in some cases. We believe these bans are relatively commonplace in contracts yet serve no benefit to effective market functioning. A ban on assignment clauses in a debtors' terms of sale tend to be in place because of historic and unrevised contractual arrangements.

30. Therefore, an intervention is needed to nullify ban on assignment clauses so that small and medium sized businesses can use their accounts receivable as collateral for invoice financing.

[2] 19 respondents responded that it would be helpful, 12 that it would not and 6 responses were inconclusive

31. Despite the restrictions imposed by ban on assignment clauses, the invoice financing sector is still growing. Invoice financing has grown in recent years. According to recent figures from the Asset Based Finance Association, an average of £17.5 billion of asset based finance is being used by UK businesses at any one time in the last year preceding 31 March 2014. This is up 9.4% from 2012/13 average value and up 29% from 2009/10. ABFA estimates that 80% of asset based finance is invoice finance. [3]

32. Invoice finance can enable those who might otherwise struggle to obtain debt funding to secure external finance, especially those small and medium sized businesses that may have no assets other than their trade receivables. This is because once the trade receivables have been assigned to the third party financer, the risk of the loan is mainly attached to the credit worthiness of the business's debtor rather than the assignee (i.e. the likelihood of the debtor paying the assigned debt rather than the likelihood of the supplier being able to repay a loan). The total advances for invoice finance stand at 15.3 billion at the end of June 2014[4] and have grown 9% compared to the same period in the previous year; this statistics include the UK and Irish markets.

33. It is possible for invoice financers to find 'work-rounds' to overcome the problems presented by bans on assignment. However, these work-rounds are primarily designed to mitigate the risks borne by the third party financer and either result in additional cost and time in providing that finance or result in a reduction of the finance that can be made available to assignors.

34. Although it may possible for a third party invoice and assignor to obtain an outright waiver of a ban on the assignment of trade receivables, anecdotal evidence suggests that many smaller businesses are reluctant to approach their debtor to request a waiver. We understand that this is because small and medium sized businesses are concerned that there is a stigma attached to invoice financing – that invoice financers are seen as being 'lenders of last resort' – and that debtors will think that they are in danger of insolvency and so will look to terminate the commercial relationship to secure their supply chain. This has been borne out by conversations that we have had with large UK business debtors, a number of whom have indicated that they would perceive a request for a waiver from a supplier to access invoice financing as a cause for concern over the financial stability of that supplier.

35. Furthermore, even where a waiver is successfully obtained or a work-round successfully implemented, the possibility of bans of assignment still impact on the provision of finance. In most instances, it is impractical for an invoice financer to check whether or not every single invoice assigned is subject to a contractual ban on assignment.

[3] http://www.abfa.org.uk/news/2014/May/pressrelease270514.asp

[4] (Q2 2014, ABFA industry statistics). This includes the UK and Irish market.

36. We believe that nullifying bans on assignment would therefore;
    - save on costs for financers to obtain waivers;
    - save on the costs for financers to obtain work-arounds and;
    - decrease the risk for financers lending money to suppliers.

37. The policy should therefore provide a suitable balance between the principle of freedom of contract and the ability to transfer the ownership of property that both allows the free flow of intangibles through fair trade, but that also gives due consideration to the legitimate interests and protection of debtors. We will consult to ensure that the policy meets this objective.

Alternatives to Legislation

38. We have considered alternative options other than legislating to nullify ban on assignment of trade receivables. We could consider offering guidance to businesses on the merits of nullifying ban on assignment of trade receivable clauses or request that businesses join a voluntary code. These measures would not compel businesses to nullify these clauses however, and could create a disjointed effort to resolve the problem.

39. We have therefore concluded that the only through legislation will we be able to remove this contractual barrier.

Policy objective and options

40. The aim of this policy will be to remove a contractual barrier to invoice financing and improve the accessibility for businesses to gain this type of finance. The objective of the policy is to help businesses lacking the sorts of assets that usually serve as collateral for a bank loan to access invoice financing. The aim of the policy is to achieve this by nullifying bans on the assignment of trade receivables which currently act as a barrier to invoice finance for businesses.

41. We are aware that the functioning of some financial markets is dependent on the concept of non-assignment. For instance, in the case of derivative products between the debtor and the creditor, a ban on assignment may compromise mutuality for set off purposes. Again, insurance policies covering loss of or damage to property are made non-assignable by the recipient of the insurance policy because that would have a substantial effect on the risk of the insurer. We will ensure that any policy intervention does not have an adverse impact on the functioning of such financial products.

Description of options considered

42. Four high level policy options have been considered:
    a. Option 0: Do nothing
    b. Option 1: Override bans on the assignment of trade receivables for goods and services (preferred option)
    c. Option 2: provide that terms are ineffective in relation to certain parties

d. Option 3: provide that such terms are effective only in relation to certain persons for certain purposes

We believe option 1 is the best fit to achieve our policy objectives, and will be the easiest to implement and for businesses and invoice financers to understand. We will plan to consult on this option.

Option 0: Do nothing

Proposal

43. Ban on assignments on trade receivables is currently legitimate and legal in a debtor's terms of sale. It allows debtors to write clauses in their terms of sale which prevent suppliers from assigning their trade receivables. This option would propose not to change this

Option 1 (Preferred option): override bans on the assignment of trade receivables for goods and services

Proposal

44. Under this option, we would provide that 'ban on assignment' of trade receivables for goods and services terms have no effect at all. This would allow for the outright nullification of bans on assignment of trade receivables only.

45. The measure would provide an exemption to ensure that contracts for financial products or services could be outside the scope of the nullification. The measure would include sufficient flexibility to allow certain financial services to be included within scope of the anti-assignment regulations if, following consultation, it is thought best to do so.

Option 2: Provide that terms are ineffective in relation to certain parties

Proposal

46. This option would make the assignment ineffective in relation to certain finance lenders, for example, it could provide that the only financers to whom assignments can be transferred to are invoice financiers. This would limit the institutions that could offer invoice financing, narrowing down the available providers to those who specifically offer invoice finance.

Option 3: provide that such terms are effective only in relation to certain persons for certain purposes

Proposal

47. Under this option the nullification of ban on assignment for trade receivables would still be in place as is the case in option one. However, there would be additional terms to protect a debtor if damages are incurred by an assignment,

e.g. providing that damages are payable for assigning in breach of a term, without affecting the validity of the assignment or the interests of the assignee.

Cost and benefits of options

48. In order to gather evidence of the impact of these proposals on UK businesses, individuals, the public sector, and to inform thinking around policy and implementation, BIS has used multiple approaches for data gathering. This includes:

- A online survey aimed at large firms see Annex B for methodology
- an online survey distributed to Asset Based Finance Association (ABFA) members (see Annex B for the methodology);
- face to face meetings with academic researchers, invoice financers, debtors, suppliers and business representative bodies.
- Publicly available industry data.
- International comparisons

The results gathered from these approaches are used to inform the analysis below. For the Final Stage Impact Assessment we will continue to develop the evidence base and provide further analysis. We intend to test our assumptions made on the impacts of the policy option through our consultation and stakeholder meetings.

Option 0: Do nothing

49. The ‘Do nothing’ option will not meet the policy objectives which is to help firms lacking the sorts of assets that usually serve as collateral for a bank loan to access alternative forms of external finance. It is likely that the ban on assignments will remain under this option because businesses are not obligated to review their contractual terms of payment, therefore historic ban on assignment clauses may not be removed.

Costs / Benefits

50. There would be no additional costs and benefits associated with this do-nothing option.

Option 1: Override bans on the assignment of trade receivables for goods and services (preferred option)

Costs and benefits

Firms in Scope

51. We propose that the nullification will apply to all UK law contracts. However, not all UK Law contracts have a ban on assignment clause in them and so this nullification will only impact those contracts that contain these specific clauses.

52. There is no evidence available on the proportion of contracts that contain a ban on assignment clause. However, as mentioned earlier in paragraph 8 our survey of ABFA members found that 100% of respondents that offer factoring services and 93% of respondents that offer invoice discounting have come across ban on assignment clauses over the last twelve months in the context of them providing funding. Also the non-representative survey aimed at large firms showed 30% of the 33 responses said they did include ban on assignment in their contract and of those who said yes minus one respondent who did not answer the question 56% said it applied to 96% -100% of their contracts.

53. The three main groups that will be most affected by the nullification will be
    a. Suppliers
    b. Debtors - with a ban of assignment clause in their contracts
    c. Invoice financers

54. Through stakeholder engagement ABFA have informed us that they have 31 UK members and 3 Republic of Ireland Members who provide factoring, invoice discounting and Asset Based lending and cover approximately 95% of the value of UK and Irish market.

55. There is not a definite answer on how many other firms may provide invoice financing who are not members of ABFA. However, we are aware of some such as some international banks and some smaller firms. To provide a sensible estimate of total number of firms in this market we have assumed that there will be an additional 16 firms which is an extra 50% of the number of UK ABFA members. Therefore, our <u>best</u> estimate of the number of UK invoice financers is 47. In discussions with the British Business Bank this seems to be a sensible estimate.

56. We know there are at least 31 invoice financers as they are members of ABFA. Therefore our <u>low</u> estimate will be 31 firms. For our <u>high</u> estimate we will assume that there are an additional 23 firms which is an extra 75% of the number of UK ABFA members bringing the total to 54 invoice financers.

57. In the online survey distributed to ABFA members we asked 'Have you come across ban on assignment in the last twelve months in the context of providing funding through [factoring/Invoice discounting]?' This question was asked separately to members who said they offered invoice discounting and to those members who said they offered factoring (see Annex A for definitions).

58. 15 responded amongst those who offer invoice discounting while 17 responded amongst those who offer factoring. 93% of the firms who offer invoice discounting have come across a ban on assignments, while 100% of the firms who offer factoring have come across a ban on assignments.

59. This indicates that the vast majority of invoice financers have an awareness of the ban on assignments.

Consultation questions to Invoice financers

Do you have any evidence on the proportion of contracts that contain a ban on assignment?

Do you agree with our estimate that there are 47 invoice financers in the UK market? Do you have any evidence that could help refine this assumption?

Do you agree with our assumption that the vast majority of invoice financers already have an awareness of the ban on assignment of trade receivables?

Consultation questions to all

Do you agree that ban on invoice assignment clauses are unintentionally written into contracts? These could be included to prevent assignment related to sub-contracting.

Costs

60. The costs that business in scope may face due to the nullification of the ban can be split into transition costs and recurring costs. Transition costs are one off costs that relate to the implementation of the measure whereas recurring costs are those that are likely to reoccur for the time that the policy measure is in force.

61. The transition costs for this policy option will be the costs for nullifying the ban and the administrative burden including the familiarisation with administrative requirements.

62. Under this option, we nullifying a clause in a contract and therefore do not expect that there to be any ongoing cost.

Consultation Question to all

Do you agree with the assumption that there will be no on-going costs

Cost of nullification to Debtors

Transition costs

Cost of nullification to suppliers

63. The measure will make the ban on assignment clause invalid, but will not require any party to retrospectively revise contracts between each other as it does not necessitate a change of contracts.

64. The calculation of the risk to lending is a burden for the invoice financer and not the supplier. There are no additional burdens to the supplier; in fact, the chances of a supplier being granted invoice financer have increased. For the supplier the

change will be very easy to understand, especially as it is an outright nullification.

Consultation questions to suppliers of contracts that include BOA:

Do you agree with our assumption that the transition costs of the nullification for ban on assignment of trade receivables will be negligible for suppliers? Do you have any evidence that could help to refine this assumption?

65. Anecdotal evidence suggests that most bans on assignments are historic and are not intentionally written into contracts. We envisage that the ban on assignment clause in contracts will remain but will become legally invalid. This will mean that debtors will not be obligated to retrospectively revise their contracts.

66. Based on our informal consultations with industry experts and businesses, we do not believe that an outright nullification of bans on the assignment of trade receivables as proposed will impose a significant burden on business debtors or deny them contractual freedom to reserve commercial confidentiality, etc.

67. In the survey aimed at large firms we asked those respondents who said they did include a ban on assignment in their contracts ‘What level of resource would be incurred by your organisation if these ‘bans on the assignment’ were made legally invalid?’. The table below shows the responses received

Table 1 Responses to the survey question: What level of resource would be incurred by your organisation if these ‘bans on the assignment’ were made legally invalid?

Answer choices	Responses
Very low	1 (11%)
Low	2 (22%)
Medium	2 (22%)
High	2 (22%)
Very High	0 (0%)
Don’t know	2 (22%)

Total responses 9

68. The survey asked those who responded “high”, “very high” or “don’t know” ‘what level of resource would be incurred by your organisation if these ‘bans on the assignment’ were made legally invalid?’ We only received 3 responses, one of which said it cannot be assessed; another misinterpreted the policy as they believed it would impact on the ability of a business to restrict the supplier from sub-contracting to a third party (which the regulations would not allow). The third said a number of its departments will be impacted but does not explain how.

69. Using a combination of the survey results gathered and policy reasoning informed by expert advice on this area, we interpreted the cost as being

negligible for debtors in this instance. We will of course challenge this assumption in our consultation.

Consultation questions to debtors

Do you agree that you will not need to retrospectively revise contracts?

Do you agree that an outright nullification of bans of assignment of trade receivables as proposed will not impose a significant burden on business debtors or deny them contractual freedom to reserve commercial confidentially etc?

Do you agree with our assumption that the transition costs of the nullification for ban on assignment of trade receivables will be negligible for debtors? Do you have any evidence that could help refine this assumption?

Cost of nullification to invoice financers

70. As the ban on assignment clause will be nullified we envisage that the clauses will remain in contracts but will become legally invalid. We therefore assume there will be no costs associated with nullifying these clauses.

71. In the survey to ABFA members we asked "*what level of resource would be incurred by your organisation if these 'bans on assignment' were made legally invalid*?" There were 19 responses to the question. 53% (10) of respondents said that resources would be freed up, 11% (2) (said there would be no impact on resources, 26% (5) said a very low level of resources would be required and 11% (2) said the level of resource incurred would be low. The respondents were asked to briefly explain why but with limited response. Those who said it would free up resources suggested that *"it would free up time of people at all levels"* and *"reduce risk profiling"*.

72. With 64% of respondents saying that there would be either no impact or that it would be positive, and the remainder saying the impact would be low or very low, we assume that there will be a negligible cost of nullifying the clause in the contract.

Consultation Questions to invoice financers

Do you agree with our assumption that the transition costs of the nullification for ban on assignment of trade receivables will be negligible for invoice financers? Do you have any evidence that could help refine this assumption?

Familiarisation costs

73. Firms may need to become familiar with the change in law and how this affects them. The familiarisation cost will include any additional management time needed to understand the change in the law and the impacts on contracts.

74. We believe that the nullification is the most significant change to invoice financers because the change to the law will have the largest impact on their calculations of lending risk.

Familiarisation costs to suppliers

75. Most suppliers have a limited awareness of a ban on assignment clauses before they seek finance from invoice financers. Suppliers will not need to gain new knowledge in order to choose invoice financing as a lending option.

76. The calculation of the risk to lending is a burden for the invoice financer and not the supplier. There are no additional burdens to the supplier; in fact, the chances of a supplier being granted a loan have increased. For the supplier the change will be very easy to understand, especially as it is an outright nullification.

Consultation question to suppliers

Do you agree with our assumption that most suppliers have a limited awareness of a ban on assignment clauses before they seek finance from invoice financers?

Do you agree with our assumption that the familiarisation costs of the nullification for ban on assignment of trade receivables will be negligible for suppliers? Do you have any evidence that could help refine this assumption?

Familiarisation costs to Debtors

77. Anecdotal evidence suggests that most bans on assignments are historic and are not intentionally written into contracts. We envisage that the ban on assignment clause in contracts will remain but will become legally invalid. This will mean that debtors will not be obligated to retrospectively revise their contracts as a familiarisation to them.

Consultation question to Debtors

Do you agree with our assumption that the familiarisation costs of the nullification for ban on assignment of trade receivables will be negligible for suppliers?

Familiarisation Costs to invoice financers

78. The survey of ABFA members asked the question: *"What level of personnel would be required to become familiarised with the change in the law to nullify the effects of bans on assignment of trade receivables?"* There were 19 responses to this question and some respondents selected more than one answer choice. As Table 2 below shows the answer choices selected by the respondents.

Table 2: Responses to survey question '*What level of personnel would be required to become familiarised with the change in the law to nullify the effects of bans on assignment of trade receivables?"*

Level of personnel	Number of times answer choice was selected
Managers	17 (89%)
Directors and senior officials	15 (79)%
Professional occupations	10 (53%)
Associate professional and technical occupations	8 (42%)
Administrative and secretarial occupations	6 (32%)
Sales and customer service occupations	5 (26%)
Skilled trades occupations	1 (5%)

Note that percentages exceed 100% as firms provided more than one response

79. The survey then asked "*Approximately how long do you think it would take for that person to become familiarised with changes in the law?"* There were 19 responses to this question, the table below shows the distribution of responses.

Table 3: Responses to survey question "*Approximately how long do you think it would take for that person to become familiarised with changes in the law?"*

Length of time taken to become familiar with changes in the law	Number of responses
0-10 minutes	1 (5%)
11-30 minutes	5 (26%)
31-45 minutes	5 (26%)
46-60 minutes	5 (26%)
1 hour to 2 hours	3 (16%)

80. As shown in the table 3 above there was no conclusive estimated time taken for the person to become familiar with the change in the law. As 5% of respondents (1 member) indicated that they think familiarisation will take 5-10 minutes, we have chosen **10 minutes** as our lower estimate. Similarly, as the survey received 3 responses for the 1 to 2 hours time-bracket we have chosen the midpoint of the time bracket, 90 minutes, as our high estimate. To arrive at our best estimate, we used the midpoint of each time range weighted by the number of responses to provide us a weighted average, the resultant average was **43 minutes**.

81. We have assumed that other staff will only need to know that a ban on assignment clause is no longer valid and should not be taken into consideration for the assessment of invoice finance. We assume that it will be a very low burden to distribute the message across an invoice financer's organisation, such as an email.

The one off familiarisation cost:

82. Utilising the pieces of data as explained above extracted from the survey of ABFA members we can estimate the one off cost of familiarisation.
We have assumed:

a) The level of employees who are responsible are corporate managers and directors
b) It will take a manager approximately 43 minutes to familiarise themselves with the change in the contracts. For the purposes of the calculation we have converted the 43 minutes into a proportion of an hour, 43 minutes is the equivalent to 0.72 of an hour (43 minutes/60 minutes).
c) There are 47 firms in scope of the policy (best estimate) as previously outlined in Paragraph 51.

83. Using the Annual Survey of Hours and Earnings, 2013 provisional results[5] the median hourly wage excluding overtime of full-time corporate managers and directors is £21.25. This hourly rate is then uprated by 17.8% to account for employers' non-wage costs[6]; the hourly cost per employer is therefore estimated to be £25.03.

Therefore, to estimate the total cost of familiarisation the following equation is used:

Invoice financers (best estimate) x Hours x cost per hour = 47 x 0.72[7] x £25.03 = **£843**

A sensitivity analysis of this estimate using a high estimate of 90 minutes and 54 invoice financers and a low estimate of 10 minutes and 31 invoice financers estimates a range of just under £2030 to just under £130.

Consultation Question to invoice financers

Do you agree that a corporate manager or a director would be required to become familiar with the change?

Do you agree with our assumption that other staff will only need to know that a BOA is no longer valid and should not be taken into consideration for the assessment of invoice finance?

Do you also agree that it will **be a very low burden to distribute the message across an invoice financer's organisation, such as an email?**

[5] http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcm%3A77-328216. Table 14.6a, full time employee jobs, median.
[6] This estimate is based on Eurostat figures for employers' labour costs and non-wage costs in the UK, 2012, for the whole economy excluding agriculture and public administration.
[7] 43 minutes is equivalent to 0.72hours

Do you agree with our best estimate that it would take 43 minutes for a corporate manager or director to familiarise themselves with the change.
Do you have any evidence that could help to refine this estimate?

Benefits

84. In this IA we have identified, described and where possible monetised the benefits. This section will identify quantitative benefits to the financer. We used the results of the ABFA members' survey to ask what the impact of ban on assignments for both types of invoice financing.

Benefits to Financers

85. We split benefits into two parts; **administration costs** (cost savings from waivers and workarounds) and **potential additional funding**.

Administration costs

86. Benefits will arise because invoice financers will no longer incur administration costs for waivers and workarounds which are sometimes currently required when they come across ban on assignment clauses in invoices. To monetise the benefit, we estimate how many waivers/workarounds there are in a year and how much they cost, we begin with waivers which factors may seek when they come across a ban on assignment.

Consultation Question to invoice financers

Do you agree that nullifying ban on assignment of trade receivable clauses will remove the administrative cost of waivers and work arounds*?*

Factoring- waivers

87. As explained previously in the IA the best estimate of the number of invoice financers is 47 with a low estimate of 31 and a high estimate of 54. However not all invoice financers will offer both factoring and invoice discounting. To find the proportion of invoice financers that offer factoring the survey of ABFA members asked 'Does your organisation offer factoring?' Of the 20 responses received 90% said they did offer factoring.

88. We make the simplifying assumption that this proportion also applies to the entire invoice finance market. Therefore our best estimate of invoice financers who offer factoring is 42 (90% of 47) with a range of 28 - 49.

89. The survey asked those respondents who said they offered factoring 'Have you come across ban on assignment in the last twelve months in the context of providing funding through factoring?' 100% of the 17 responses received said yes.

90. The survey then asked ‘Generally, what is the impact of a ban on assignment on your decision to offer factoring?’ Respondents were asked to select all the answer choices that applied to their organisation. The table below shows the answer choices selected by the 17 respondents.

Table 4: Answer choices selected by those respondents who offer factoring, ‘Generally, what is the impact of a ban on assignment on your decision to offer factoring?’

	Number of times answer choice selected
No difference compared with contracts without a ban	1 (6%)
Try to obtain a waiver	10 (59%)
Straight refusal to offer factoring (exclude the debts)	7 (41%)
Reduce funding available against contracts subject to ban on assignment	15 (88%)
Increase in rates to reflect additional risk	4 (24%)
Requirement for additional security	8 (47%)
Other	1 (6%)

Brackets contain the percentage of respondents that selected the answer

91. As suggested by the survey results shown, if there is a ban on assignment clause present, 59% of respondents may try to obtain a waiver.

92. Therefore, applying this percentage to the estimated number of invoice financers who offer factoring estimates that 25 (59% of 42) factors may try to obtain a waiver if they come across a ban on assignment.

93. Waivers could potentially be sought on each individual invoice or by each individual client. Due to the very high volume of invoices that factors deal with and anecdotal evidence we believe it is unlikely that a waiver is sought for every invoice. We have therefore made the simplifying assumption that invoice financers only seek a waiver for each client. Therefore, waivers are agreed per client rather than on an invoice by invoice basis as this would result in an extremely large number of waivers, which is unrealistic.

94. However we are aware that for some clients factors may need to seek more than one waiver as the client may have contracts with a range of different customers. However, there is currently no evidence on the average number of waivers factors may seek per client. Therefore the simplifying assumption of one waiver per client may result in an underestimate of the benefits. We will test the assumption in paragraph 90 and 91 for our final Impact Assessment.

95. The survey asked those respondents who said their organisation offers factoring to approximate the number of clients they had provided factoring for in the last twelve months. On average over the 18 responses received approximately 1,310 clients were provided with factoring in the last twelve months.

96. Not all clients may have a ban of assignment in their contracts. To estimate the proportion of clients that may have a ban on assignment the survey asked 'what was the approximate proportion by value of total assignments that you assessed for factoring in the last twelve months that included ban on assignment?' If respondents did not know the proportion by value they were asked to approximate the proportion by number of invoices. The table below shows the responses

Table 5: Responses to survey question, 'what was the approximate proportion by value of total assignments that you assessed for factoring in the last twelve months that included ban on assignment?'

	Number of Responses – approximated proportion by value	Number of responses – approximated proportion by number
0-25%	13	4
26-50%	1	0
51-75%	0	1
76-95%	0	0
96-100%	0	0
Weighted average using midpoints of categories	14.3%	22.5%

(Note two respondents provided answers both by value and by number

97. The survey showed that the weighted average using the midpoints of the answer categories suggests 14.3% of total assignment by value and 22.5% of total assignment by number which were assessed for factoring in the last twelve months included a ban on assignment.

98. To exercise caution over our estimated benefits we have taken the lower estimate of the proportion of total assignments that include a ban on assignment. Although this represents proportion of total assignments by value we have made the simplifying assumption that this can be applied to the number of clients to estimate the proportion of clients that are likely to have a ban on assignment. Therefore, we estimate approximately that 14% of factors' clients will have a ban on assignment.

99. Using all this information provided from the survey it is possible to estimate the number of waivers that could potentially be sought each year. We have assumed

that this does not fluctuate significantly annually. See figure one for an explanation of the calculation.

Figure 1: Calculation to estimate the total number of waivers sought by factors each year

Step one: estimate the number of businesses offering factoring

Estimated number of invoice financers	x	Proportion who offer factoring	=	Estimated number of businesses offering factoring
47		90%		42

Step two: Estimate number of businesses offering factoring that come across a ban on assignment

Estimated number of businesses offering factoring	x	% who came across BOA over last 12 months	=	Estimated number of businesses offering factoring who came across BOA
42		100%		42

Step three: Estimate number of businesses offering factoring that may consider seeking a waiver in response to a Ban on Assignment

Estimated number of Financers who come across BOA	x	Proportion who may consider seeking a waiver	=	Estimated number of businesses offering factoring who may seek waivers
42		59%		25

Step four: estimate number of waivers sought in last twelve months

Estimated number of businesses offering factoring who may seek waivers	x	Average number of clients	x	Estimated proportion of clients that have a BOA	=	Estimated number of waivers sought each year
25		1310		14.3%		4679

100. As Figure one shows it is estimated that in total factors seek 4679 waivers each year. A sensitivity analysis of this estimate using a high estimate of 54 invoice financers and a low estimate 31 invoice financers estimates a range of 3181 to 5427 waivers.

Consultation Questions to invoice financers who offer factoring

Do you agree with our estimate that 90% of invoice financers offer factoring?

Do you agree that 100% of invoice financers who other factoring have come across a ban in assignment in the last 12 months?

Do you agree that around 59% of invoice financers who offer factoring and who came across ban on assignment would as one of their options try to obtain a waiver?

Do you agree that waivers are sought for each client rather than on individual invoices i.e. one waiver per client?

Do you have any evidence on the average number of waivers factors may seek per client?

Do you agree the average Factor has around 1310 clients in the last 12 months?

Do you agree that around 14% of an invoice factors' clients will have a ban on assignment?

Do you agree with our calculation to estimate the number of waivers that could potentially be sought each year? Do you agree with the number of waivers estimated?

Do you agree with our assumption that the number of waivers sought will not fluctuate significantly annually?

Do you have any evidence that could help refine this estimate?

Cost of waiver

101. To estimate the cost of waiver the survey asked questions on the impact of arranging one. Firstly it asked those respondents who offer factoring 'who is the onus on to arrange a waiver'. The 17 responses 59% (10) said it was joint, 29% (5) said the onus was on the applicant of factoring and 12% (2) said the onus was on their organisation. In calculating the benefits we have only calculated the cost to the invoice financer because our survey only collected information from invoice financers and not the applicants. This is because our survey was aimed at ABFA members and therefore did not collect any information on the costs of waivers incurred by those applying for finance; this may lead to an underestimate of benefits.

102. The survey asked factors 'what on average is the resource needed to obtain a waiver' this was an open-ended question and we received a variety of responses; not all responses gave numerical estimates of hours. Responses ranged from 3 hours, half a day, 1 day, 5 days to weeks. What is also shown by the data collected is that the timing resource required does depend on the complexity of the case.

103. We believe that some respondents to this question interpreted it slightly differently and reported the time from start to finish of obtaining a waiver rather than the actual hours of work required, It is more likely that the lower estimates where actual time of work rather than the time of the process, Through the survey responses it is clear that firms do spend a lot of time on waivers but it is important to be proportional in our analysis and not overstate how much money they spend on them. It is important to bear in mind that if the costs were really high firms would not apply for a waiver in the first place.

104. The lowest reported answer provided in those responses to the survey who quantified the number of hours was 3 hours. Therefore our low estimate assumes that it takes 3 hours. Although some responses said days or weeks we believe it is unlikely this is actually hours of work required, therefore, we have assumed in our high estimate that it would take 7 hours.

105. The best estimate is 5 hours this is the mid-point between the high and low estimate. This could either be spread across the long process or concentrated across a few days.

106. Not many responses specified what staff member would have to perform the task to arrange the waiver; however a couple of responses did say they would need legal advice, a solicitor or a legal clerk. Therefore we have assumed that it would be a solicitor who would have to arrange the waiver.

107. Using the Annual Survey of Hours and Earnings 2013 provisional results[8] the median hourly pay excluding overtime for full time solicitor has been estimated to be £21.05. This hourly rate is then uprated by 17.8% to account for employers' non-wage costs[9]; the hourly cost is therefore estimated to be £24.80.

108. Therefore the estimate cost of a waiver is:

Estimated cost of a waiver: Estimated number of hours needed to obtain a waiver x hourly wage of a solicitor = Best estimate 5 hours * £24.80 = £124

109. A sensitivity analysis of this using a high estimate of 7 hours and a low estimate of 3 hours provides a range of £173.6 and £74.4

[8] http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcm%3A77-328216. Table 14.6a, full time employee jobs, median.

[9] This estimate is based on Eurostat figures for employers' labour costs and non-wage costs in the UK, 2012, for the whole economy excluding agriculture and public administration.

110. Therefore to estimate the total cost of waivers sought by factors we apply the estimated cost of each waiver to the estimated number of waivers from figure one.

Table 6: summary of the estimated costs of waivers per year.

Estimate	Factoring
Low estimate	£0.2m
Best estimate	£0.6m
High estimate	*£0.9m*

111. As table 6 shows that it is estimated each year waivers cost factors £0.6m (best estimate). Low estimate is estimated using 3181 waivers with a cost of £74.4 and high estimate is estimated using 5427 waivers with a cost of £173.6.

112. Therefore if ban on assignments are nullified this removes the need for waivers and therefore factors no longer need to spend this resource. We have made the simplifying assumption that the number of waiver sought will not significantly differ annually.

Consultation Question to invoice financers who offer factoring?

Do you agree with our best estimate that it takes 5 man hours of work for a waiver to be issued?

Do you agree that the work to issue a waiver is undertaken by a solicitor? If not who do you think would undertake the work?

Do you agree with our calculation for the cost of a waiver? Do you agree with the average cost of a waiver best estimate of £124?

Do you agree with our final calculation? Do you have any evidence that could help refine this calculation?

Success of waivers

The survey indicates that not all waivers are successful. Therefore, if ban on assignment was removed potential finance could be unlocked which was previously held back by unsuccessful waiver applications.

Invoice Discounting - Workarounds

113. In the case of invoice discounting there are often workarounds which mitigate against the risk of retrieving monies owed to a client in the case the insolvency of that client. This can involve the finance provider setting up a separate trust account into which they must require monies owed from the customer to be paid, and establishing a power of attorney to pursue monies owed in trade debt to the client in the case of insolvency to ensure that the financer can secure payment. These workarounds take up resource to arrange them and therefore if ban on

assignment are nullified, there will be no need for these workarounds and financers are able to provide their services at a reduced cost to the supplier due to administrative savings.

114. As explained previously not all invoice financers will offer both factoring and invoice discounting. In the survey of ABFA members out of 19 responses to the question on whether their organisation offers invoice discounting 79% said their organisations do offer invoice discounting.

115. We again make the simplifying assumption that this proportion also applies to the entire invoice finance market. Therefore our best estimate of invoice financers who offer invoice discounting is 37 (79% of 47) with a range of 24 - 43.

116. The survey asked those respondents who said they offered invoice discounting ‘Have you come across ban on assignment in the last twelve months in the context of providing funding through factoring?’ to which 93% of the 15 responses received said yes. Therefore applying this to the estimate of invoice discounters suggests that 34 invoice discounters will come across ban on assignments.

117. The survey asked those invoice financers that said their organisation offered invoice discounting ‘Do you use workarounds to mitigate against the risk of retrieving monies owed to a client in the case of the insolvency of that client?’ There were 15 responses some of whom selected more than one answer choice.

Table 7: Answer choices selected by those respondents who offer invoice discounting to the survey question, ‘Do you use workarounds to mitigate against the risk of retrieving monies owed to a client in the case of the insolvency of that client?’

	Number of times answer choice selected
None	2 (13%)
Requirement that proceeds be paid into a separate trust account	9 (60%)
Additional debenture or guarantees	10 (67%)
Declaration of trust of contract rights	2 (13%)
Declaration of trust of proceeds	5 (33%)

118. As shown by table 7 a majority of invoice discounters (87%) responded that they do use a workarounds of some type to mitigate against the risk of retrieving monies owed to a client in the case of insolvency of that client.

119. The survey asked those respondents who said their organisation offers invoice discounting to approximate the number of clients they had provided invoice discounting for in the last twelve months. On average over the 14 responses received approximately 589 clients were provided with factoring in the last twelve months.

120. However not all clients may have a ban of assignment in their contracts. To estimate the proportion of clients that may have a ban on assignment the survey asked ‘what was the approximate proportion by value of total assignments that you assessed for factoring in the last twelve months that included ban on assignment?’ The table below shows the responses.

Table 8: Survey responses to ‘what was the approximate proportion by value of total assignments that you assessed for factoring in the last twelve months that included ban on assignment?’

Available answer choices	Number of Responses – approximated proportion by value
0-25%	10
26-50%	3
51-75%	1
76-100%	0
Weighted average using midpoints of categories	21%

121. The survey showed that the weighted average using the midpoints of the answer categories suggests 21% of total assignment by value which were assessed for invoice discounting in the last twelve months included a ban on assignment. Therefore we estimate approximately 21% of an invoice discounters clients will have a ban on assignment. Although this represents proportion of total assignments by value we have made the simplifying assumption that this can be applied to the number of clients to estimate the proportion of clients that are likely to have a ban on assignment. Therefore, we estimate approximately that 21% of invoice discounter’s clients will have a ban on assignment.

122. Using all this information provided from the survey it is possible to estimate the number of workarounds that could potentially be sought each year. We have assumed that this does not fluctuate significantly annually. See figure two for an explanation of the calculation.

Figure 2: Calculation to estimate the total number of work arounds sought by invoice discounting each year

Step one: estimate the number of invoice discounters

Estimated number of invoice financers	x	Proportion who offer invoice discounters	=	Estimated number of invoice discounters
47		79%		37

Step two: Estimate number of invoice discounters that come across a ban on assignment

Estimated number of invoice discounters	x	% who came across BOA over last 12 months	=	Estimated number of invoice discounters who came across BOA
37		93%		35

Step three: Estimate number of invoice discounters that may consider seeking a work around in response to a Ban on Assignment

Estimated number of invoice discounters who come across BOA	x	Proportion who may consider obtaining a workaround	=	Estimated number of invoice discounters who may obtain workarounds
35		87%		30

Step four: estimate number of work arounds sought in last twelve months

Estimated no. of invoice discounters who may seek workarounds	x	Average number of clients	x	Estimated proportion of clients that have a BOA	=	Estimated number of workarounds sought each year
30		589		21%		3786

123. As Figure 2 shows it is estimated that in total invoice discounters seek 3786 workarounds each year. A sensitivity analysis of this estimate using a high estimate of 54 invoice financers and a low estimate 31 invoice financers estimates a range of 2398 to 4418 waivers.

124. To estimate the cost of a workaround the survey asked questions on the impact of arranging one. Firstly it asked those respondents who offer invoice discounting ‘who is the onus on to arrange a workaround’ of the 14 responses 71% said it was joint, 29% said the onus was on their organisation and 0% said the onus was on the applicant of invoice discounting. In calculating the benefits we have only calculated the cost to the invoice financer because our survey only collected information from invoice financers and not the applicants. This is because our survey was aimed at ABFA members and therefore did not collect any information on the costs of workarounds incurred by those applying for finance; this may lead to an underestimate of benefits.

125. The Survey also asked what level of resource was needed to establish the workaround. Responses to this question were varied; one member stated that

workarounds are normal practice so require no additional resource; 3 hours; half a man day; days; and another reported legal costs as high as £1000. Because of the wide range of answers given, we did not feel it possible to draw on this to provide an estimate of resource leads.

126. As a waiver can be used as a workaround, we have made comparisons with the equivalent question for waivers and make a simplifying assumption. We assume that the cost of a waiver is equivalent of the cost of a workaround for the purposes of the impact assessment.

127. Therefore to estimate the cost of workarounds per year:

Total cost of workarounds = 3786 (best estimate workarounds per year) x £124(cost per workaround)
= £0.5 million (best estimate)

128. A sensitivity analysis of this using a high estimate of 4418 workarounds with a cost of £174 per workaround and a low estimate of 2398 workarounds with a cost of 74.4 per workaround as described in paragraph £104 provides a range of £0.8m and £0.2.

129. We have made the simplifying assumption that the number of workaround sought will be significantly differ annually. We will again be testing this assumption for our final Impact Assessment.

Table 9: Total workaround costs saved each year (benefits)

Work around	Cost
Low estimate	£0.2m
Best Estimate	£0.5m
High estimate	*£0.8m*

Consultation Questions to invoice financers who offer invoice discounting

Do you agree that if ban on assignments are nullified workarounds are no longer needed and therefore will free up resources?

Do you agree with our estimate that 79% of invoice financers offer invoice discounting?

Do you agree with the estimate that 93% of invoice financers who offer invoice discounting will come across ban on assignments?

***Do you agree that 87% of invoice financers who offer invoice discounting and come across ban on assignment will use a workaround to mitigate against the risk of retrieving monies owed to a client in the case of insolvency of that client*.**

Do you agree on average an invoice financer who offers invoice discounting on average has around 589 clients?

Do you agree with the estimate that 21% of invoice discounters' clients will have a ban on assignment?

Do you agree with our calculation to estimate the number of workarounds that could potentially be sought each year? Do you agree with the best estimate of 3786 of workarounds sought each year?

Do you agree with our assumption that the number of workarounds sought will not fluctuate significantly annually?

Do you have any evidence that could help refine this estimate?

Do you agree with the assumption that the cost of a waiver is equivalent to the cost of a workaround?

Do you agree with our best estimate resource saving of workarounds to be £0.5m per year? Do you have any evidence that could help refine this estimate?

Table 10: Summary of annual monetised benefits for Option one

Cost to Financers	Low Estimate	Best Estimate	High Estimate
Factoring (waivers)	£0.2m	£0.6m	£0.9m
Invoice Discounting (workarounds)	£0.2m	£0.5m	£0.8m
Total yearly cost saved / BENEFIT	£0.4m	£1.0m	£1.7m

Additional benefits which have not been monetised

130. It is expected that the policy will lead to wider benefits around the amount of invoice finance available, the cost of invoice finance and the security required.

131. As shown in Table 1 earlier in the IA when factors were asked 'Generally, what is the impact of a ban on assignment on your decision to offer factoring?' the answer choice 'straight refusal to offer factoring' was an answer choice selected by 7 of the 17 respondents (41%), 'reduce funding available contracts subject to ban on assignment' was selected by 15 respondents (88%), 'increase in rates to reflect additional risk' was selected by 4 (24%) respondents and 'requirement for additional security' was selected by 8 (47%) respondents. Most respondents selected more than one answer choice; however this gives an indication of the types of things they may consider when they come across a ban on assignment.

132. Those respondents who said their organisation offered invoice discounting were also asked ‘Generally, what is the impact of a ban on assignment when applying for invoice discounting?’ Respondents were asked to select all the answer choices that applied to their organisation. The table below shows the answer choices selected by the 15 respondents.

Table 11: Answer choices selected by those respondents who offer invoice discounting, ‘Generally, what is the impact of a ban on assignment when applying for invoice discounting?’

	Number of times answer choice selected
No difference compared with contracts without a ban	2 (13%)
Try to obtain a waiver	8 (53%)
Try to find a workaround to mitigate possible risks associated with insolvencies	9 (60%)
The price of invoice discounting is higher	6 (40%)
The amount of funding is reduced	12 (80%)
Straight refusal to offer invoice discounting	6 (40%)

Brackets contain the percentage of respondents that selected the answer

133. As suggested by the survey results shown in the table above that if there is a ban on assignment as one of their potential responses 40% of the respondents who offer invoice discounting may increase the price of invoice discounting, 80% may reduce the funding and 40% may straight refusal to offer invoice discounting.

134. Thus, we envisage that the nullification of ban on assignments may lead to fewer straight refusals of invoice discounting and factoring, potentially a higher amount of funding available both in the case of invoice discounting and factoring, and a lower price for invoice discounting as well as decreased rates and lower security requirements for factoring. These benefits may be felt by the clients of invoice financiers; both SMEs and larger businesses who previously had a ban on assignment clause in their invoice.

135. It is very difficult to monetise this potential impact. For example although many have said straight refusal is an option they consider when they come across a ban on assignment we do not know with certainty how often this option is used. We also have no evidence for those that were given a straight refusal what the average amount of requested finance was. Although we envisage some applications may now be successful due to the nullification of ban on assignment this is not necessarily the case for all those rejected as there may be other reasons the finance application was not successful. Again for reduction in funding there is no evidence to show how many of these invoices would have

reduced funding anyway due to other reasons. We will try to improve our evidence base on the benefits extents for the final Impact Assessment.

Consultation questions to invoice financers who offer factoring

Do you agree that where a ban on assignment is present for invoice financers *who offer factoring as one of their potential responses 24% may increase rates to reflect additional risk; 88% may reduce the funding and 41% may straight refusal to offer invoice factoring?*

Has the presence of a ban on assignment ever caused your organisation to refuse funding, increase price or reduce the amount of funding available? If so what one and how often?

If the ban on assignment is nullified what do you think would be the impact on the amount of finance available or the cost of finance? Do you have any evidence about the potential impact?

Do you agree that the nullification of ban on assignment could lead to an increased amount of finance available and to a reduction in the cost of finance?

What is the average amount of an application that got straight refusal due to a ban of assignment?

How often is a ban on assignment the sole reason for a reduction in finance? If the ban on assignment is nullified how often could the full payment be offered?

Consultation Questions to invoice financers who offer invoice discounting

Do you agree that where a ban on assignment is present for invoice financers who offer invoice discounting as one of their potential responses 40% may increase the price of invoice discounting; 80% may reduce the funding and 40% may straight refusal to offer invoice discounting?

Has the presence of a ban on assignment ever caused your organisation to refuse funding, increase price or reduce the amount of funding available? If so what one and how often?

If the ban on assignment is nullified what do you think would be the impact on the amount of finance available or the cost of finance? Do you have any evidence about the potential impact?

Do you agree that the nullification of ban on assignment could lead to an increased amount of finance available and/to a reduction in the cost of finance?

What is the average amount for an application that got straight refusal due to a ban of assignment?

How often is a ban on assignment the sole reason for a reduction in finance? If the ban on assignment is nullified how often would the full amount be offered?

Option 2: Provide that terms are ineffective in relation to certain parties

136. This option (allowing assignment only to invoice finance providers) would be difficult to legislate on as ‘invoice finance’ is not itself an activity that is formally regulated by the Financial Conduct Authority. This would mean that it would be legally difficult to define those to which assignment would be permitted. An alternative to this would be to define invoice finance as an activity for which anti-assignment clauses would be invalidated. Again, this could result in definitional difficulties. This may potentially have adverse impacts on the invoice financing market.

Costs and benefits

137. Under this option we again assume that there will be no nullification costs as no contracts will need to be retrospectively changed. However, due to the complexities around when a ban on assignments is valid, we assume that more parties will need to become familiar with this policy. We assume that suppliers would need to identify invoice financers and institutions who wish to lend finance on the basis of invoices as collateral will need to know if they are classed as an invoice financer under the policy.

138. We also assume there will be ongoing costs to this policy as potentially when a supplier wants to access invoice financing they may now need to identify which institutions are invoice financers.

139. While we have not been able to qualify the costs of this option, we think it reasonable to assume that those will be higher than for options one and three.

140. Dependent on who would be classed as an invoice financer under the policy, the benefits maybe equal to our preferred option for example in the case that all 47 (best estimate) firms that we estimated may provide invoice financing currently are classed as an invoice financer. If only a selection are deemed invoice financers under the terms of the policy the benefits are reduced as those not captured are the invoice financing definition may need to continue to seek waivers and work arounds in the presence of a ban on assignment clause.

141. While we have not been able to quantify the benefits we believe it is reasonable to assume that these will be higher than option zero, but no greater than option one and three.

Consultation questions to invoice financers

Do you agree with our assumption that more parties would need to become familiar with this policy?

How much time would it take to become familiar with this change? Who would be responsible for performing this task? How will the rest of the organisation become familiar?

Do you agree suppliers would need to identify who is classed as an invoice financer before applying?

Consultation questions to all

Do you agree that there would be no nullification to any parties as no contracts would need to be retrospectively changed?

Do you agree that the costs would be higher than option one and three?

Do you agree that the benefits would have less of an impact because of the limitations of the measures to approved invoice financers?

Do you agree that the benefits of this option would be higher than zero, but no greater than option one and three?

Consultation questions to suppliers

Do you agree that you will need to identify who is classed as an invoice financer before applying? How much time will this take? Who in your organisation will be responsible who preforming this task?

Option 3: provide that such terms are effective only in relation to certain persons for certain purposes

142. This option has legal precedent in Canada. However, it could still create uncertainty to small businesses about their rights to assign. In addition, our Impact Assessment shows low levels of costs associated with introducing the prohibition on ban on assignment clauses.

Costs and benefits

143. Under this option we again assume that there will be no nullification costs as no contracts will need to be retrospectively changed. However, due to the complexities around the ability of a party to sue when damages are incurred due to an

assignment, we assume that more parties will need to become familiar with this policy thereby leading to larger costs. Businesses will also bear familiarisation costs associated with understanding terms where assignment has disadvantaged them which could surmount to considerable legal costs.

144. For those firms who were previously able to include ban on assignment clauses for the purpose of commercial protection, this policy may lead to additional on-going costs if they now need to sue for damages. Even if a legal case is successful then the firm will still bear additional costs on their time.

145. As the ban on assignment clause will be nullified as in option one, we believe that the benefits to this option will be the same as the first option.

Table 12: Summary of annual monetised benefits for Option three

Cost to Financers	Low Estimate	Best Estimate	High Estimate
Factoring (waivers)	£0.2m	£0.6m	£0.9m
Invoice Discounting (workarounds)	£0.2m	£0.5m	£0.8m
Total yearly cost saved / BENEFIT	£0.4m	£1.0m	£1.7m

146. While we have not been able to quantify the costs we believe it is reasonable to assume that these will be higher than option one and two and option zero.

Consultation questions to all

Do you agree there will be no nullification costs to all parties as no contracts will need to be retrospectively changed?

Do you agree that giving debtors the right to claim for damages by an assignment would bear a number of costs? These could be related to further familiarisation costs for the policy, potential legal costs.

Do you agree that the costs would be higher than option zero, one and two?

Do you agree that the benefits of this option would be the same as option one?

Rationale and evidence that justify the level of analysis used in the IA

147. In order to gather evidence of the impact of these proposals on UK businesses, individuals, the public sector, and to inform thinking around policy and implementation, BIS has used multiple approaches for data gathering. This includes:

- an online survey distributed to Asset Based Finance Association (ABFA) members (see Annex A for the methodology);

- an online survey aimed at large firms see Annex B for methodology
- face to face meetings with academic researchers, invoice financers, debtors, suppliers and business representative bodies.
- Publicly available industry data.
- International comparisons
- Reviewing other IAs within this area

148. The results gathered from these approaches are used to inform the analysis within the costs and benefits sections. For the Final Stage Impact Assessment we will continue to develop the evidence base and provide further analysis. We intend to test our assumptions made on the impacts of the policy option through our consultation and stakeholder meetings.

149. We sent an online survey to ABFA who distributed it across all their members. ABFA have 31 UK based (including Northern Ireland) members with another 3 Republic of Ireland members. Therefore, potentially 3 respondents from Northern Ireland could have responded to the questionnaire however we are unable to identify or filter these responses out. This survey aimed to find out what impact ban on assignment clauses have when trying to obtain invoice finance and the costs that are incurred because of them.

150. International comparisons were also limited. We engaged and researched ban on assignment measures in several countries including the US, Canada, Australia, Germany and France. There were very few datasets and only one concrete assurance from Australia that the effect of ban on assignment clauses would be reviewed in December 2014 with a final report due in January 2015.

151. We conducted a non-representative online survey aimed at large firms as part of the wider prompt payment policy development survey which contained some questions relating to ban on assignment. We received 35 valid responses.

152. We reviewed the Final Impact Assessment for banning exclusivity clauses in zero hour contracts, July 2014, IA number BISLMD002 to learn from the methodology used to assess the policy, the impacts the policy had and to identify lessons learnt.

Risks and assumptions

153. The key assumptions and risks underpinning the cost-benefit analysis are:

   a. Costs in this IA have been informed by limited information gathered from a survey of ABFA members. The survey was sent to ABFA who distributed it to their members. ABFA have 31 UK based (including Northern Ireland) members with another 3 Republic of Ireland members. Therefore, potentially 3 respondents from Northern Ireland could have responded to the questionnaire however we are unable to identify or filter these responses out. The survey is not a representative sample of all invoice financers and therefore the resulting estimations are not statistically representative but instead provide a reasonable best estimate of the likely impact of the policy.

b. The exact number of invoice financers is unknown. We do know that ABFA currently has 31 UK members which represent the majority of invoice financers. However, in discussions with ABFA we are aware there are some invoice financers which are not part of ABFA. Therefore we have conducted sensitivity analysis around this. Our best estimate is 50% additional invoice financers in the entire market and our high estimate is 75% additional invoice financers in the market. This means our low estimate assumes 31 invoice financers, best estimate assumes 47 invoice financers and our high estimate assumes 54 invoice financers.

c. ABFA statistics cover both the UK and Irish markets and this has been made clear in the IA where any statistic covers both markets. Therefore they provide an overestimate of the UK market. However, Irish members of ABFA are a small minority in terms of the overall funding provided, reducing the potential overestimate.[10]

d. This policy will not cover contracts that use Scottish law. We assume that invoice financers are national and offer invoice finance on invoices that are both UK and Scottish law therefore all invoice financers will need to become familiar with the nullification. It is unknown what proportion of contracts that are assessed by invoice financers are Scottish Law and whether ban on assignment clauses are more or less frequent in Scottish law contracts. This could lead to an under or over estimate of benefits depending upon if ban on assignment are more or less likely in Scottish law contracts and the proportion of contracts that invoice financers assess that are Scottish law. We will seek to gain further evidence on this issue for our final Impact Assessment.

e. We have assumed only invoice financers will need to become familiar with the nullification and that there will be no on-going costs in our preferred option 1. Monetisation of the costs assume the time of a particular task and employee who will be performing this task. We have assumed there are only costs to invoice financers because they need to understand the changes to the law in order to assess the risk of lending money in their market. Sensitivity analysis around the hours the tasks required has been performed; we have assumed that it will take an invoice financer 0.72 hours to become familiar.

f. Monetisation of the benefits assumes the costs associated with the waivers and workarounds are no longer incurred if ban on assignments are nullified. We have assumed that the number of waivers and workarounds sought each year will not significantly differ.

g. We have assumed for invoice discounters if they arrange a workaround they will not need a waiver. We also assume that the cost of a waiver and workaround are the same. Our best estimate is that it takes 5 hours of a

[10] In our engagement with ABFA we were told that there were three members in the Irish market.

solicitor's time to arrange a waiver or workaround with a sensitivity analysis of between 3 and 7 hours.

h. We will seek to confirm these assumptions in consultation.

Consultation Questions

Do you agree with our list of risks and assumptions? What other factors have we missed from this list?

Are there any assumptions that you do not agree with in the list above?

What proportion of you contracts are agreed under Scottish Law?

Direct costs and benefits to business calculations including OITO considerations

154. The preferred option 1 is in scope of One in Two Out as it is a new measure which regulates business. As the policy is regulatory and the direct incremental economic benefit to business exceeds the direct incremental economic cost to business the measure is classified as Zero Net Cost.

155. The quantified costs have a best estimate present value of £0.0m over a ten year period. The best estimate of the cost is estimated to be around £843 for familiarisation in the initial year by invoice financers with a range of just under £2030 to just under £130. The quantified benefits have a best estimate present value of £9.0m over a ten year period. Therefore the total Net Present Value (best estimate) is £9.0m over the ten year period.

156. This equates to an equivalent annual cost of £0m and an equivalent annual benefit of £0.8m (using the BRE calculator, 2009 prices). Therefore the equivalent annual net cost to business is estimated to be -£0.8m; however as the measure is regulatory it is classed as a Zero Net Cost.

Enforcement

157. The implementation of this measure will apply automatically to contracts agreed after the measure is brought into force. Government will not have an enforcement role as it affects contract law.

Review clause

158. Within the Small Business, Enterprise and Employment Act there is a duty to review secondary legislation as created by the Act 5 years after implementation.

Equalities impact

159. We have assessed the proposed measure against the equality duty and do not consider it to have an adverse effect on any protected group. Indeed, we

consider that these measures will have a positive effect on Black Minority, Ethnic (BME) and Women-led businesses.

160. Invoice financing is typically used to release working capital to ensure a positive and healthy cash-flow. A strong cash flow is vital in enabling businesses to raise finance and invest. The nullification of bans on assignment of trade receivables will help small and medium sized businesses maintain a healthy cash flow. According to Professor Russell Griggs, who leads the independent external review of the major banks' Appeals Process, reported that in 2012/2013 48% of declined finance applications over £25,000 were rejected on 'affordability' grounds[11] – the ability of a small business to service the debt from its existing cash-flow.[12] A 2013 report produced by the Department for Communities and Local Government[13] (DCLG) found that 'affordability is an area that disproportionality affects the 8% of Britain's 4.8 million small and medium sized businesses which are BME owned. The removal of bans on the assignment of trade receivables as a barrier to accessing finance will therefore appear to have the potential to benefit BME businesses disproportionately.

161. Specifically, the DCLG report found that BME businesses face the following challenges which make access to finance more difficult[14]:

- collateral shortages;
- poor credit worthiness (as assessed through credit-scoring);
- lack of formal savings; and
- poor financial track record

162. The report concluded that non-BME businesses were as a result 10% more likely to receive an overdraft or loan than BME businesses (87% vs. 77%).[15] One of the principle advantages of invoice financing is that it allows businesses lacking other collateral to use their trade receivables as security to gain access to finance. The measure to nullify bans on the assignment of trade receivables therefore has the potential to bring particular benefits for BEM businesses by allowing eligible businesses who lack collateral other than trade receivables or have poor credit ratings to access finance.

163. While evidence suggests that women-led businesses do not in general suffer a greater failure rate when seeking to access finance than their male-led

[11] Affordability relates to the ability of a business to service a debt. In a loan application a finance provider may chose not to award the finance as the company would not be able to make repayments during the course of the requested loan.

[12] http://www.betterbusinessfinance.co.uk/images/uploads/Annual_Report_Master_2013.pdf

[13] Ethnic Minority Businesses and Access to Finance, Department for Communities and Local Government, July 2013

[14] The report looked at the access to finance of BME businesses. Whilst inferences can be made related to affordability of the loans and the impact on affordability created by late payment, was must consider that the main report did not explicitly look at late payment.

[15] http://www.accaglobal.com/ie/en/member/accounting-business/bank-fairness.html

businesses, there is evidence that women-led businesses are less likely to seek finance in the first place because of a desire to avoid debt and discouragement from the process of applying for external finance.[16] While invoice finance may not be right for all companies, it does change the relationship with debt and may allow a more attractive form of finance for some women-led businesses, suggesting particular benefit for this protected group.

Small and micro business assessment

164. The aim of this policy will be to remove a contractual barrier to invoice financing and improve the accessibility for businesses to gain this type of finance. The policy objective is to remove barriers to finance for those businesses that want to obtain invoice financing. Nullification of bans on assignment of trade receivables will result make it easier for small and medium sized businesses to access this form of finance by removing a contractual barrier, and increase the availability of funding available by reducing the risks faced by financers of non-payment.

165. This will benefit all businesses wishing to obtain invoice financing, but particularly small and medium sized businesses as invoice financing can provide businesses with a source of finance which might otherwise be declined a loan due to a lack of collateral. Low collateral is a problem typically faced by small and start-up businesses as they will lack significant assets such as warehouses, large stock, machinery, etc.

166. A lack of significant collateral is perhaps the most significant obstacle facing businesses needing finance. In February 2013, a report by the Durham Business School's Policy Research Group reviewing the Government's Enterprise Guarantee Scheme concluded that the scheme was providing "high" additionally because it was "allowing businesses without collateral and/or a substantive track record to access loans which they would not have received otherwise"; and of these two factors a lack of collateral was the most significant. These businesses had median collateral between £50,000-£100,000. This compared to £250,000-£500,000 for conventional borrowers.[17]

167. A nullification of bans on the assignment of trade receivables will open this form of finance to more businesses and allow the market to operate in a space that has required on-going Government intervention.

168. There may be cases where an invoice financer may be classed as small and micro and therefore may bear the familiarisation cost. However, this policy is likely to reduce the potential costs they may currently incur if they use waiver or workarounds if they come across ban on assignment clauses.

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[16] Women-led businesses Analysis from the SME Finance Monitor YEQ1 2012 An independent report by BDRC Continental, 2012

[17] Economic Evaluation of the Enterprise Finance Guarantee (EFG) Scheme, downloaded from https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/85761/13-600-economic-evaluation-of-the-efg-scheme.pdf (08/09/2014), p.44

Annex A: Definitions of the methods of Invoice Financing

Factoring

1. Factoring occurs when the supplier assigns their trade receivables to a third party financer and the financer takes responsibility for the supplier's sales ledger maintenance and all credit control collections (this might include issuing of statements/letters, telephone calls and commencement of legal procedures in the case of non-payment, etc.) – i.e. the third party financer assumes the position of the creditor in the relationship with the supplier's customers.

2. There are generally two forms of factoring – recourse and non-recourse factoring. Under non-recourse factoring, the third party finance provider assumes the risk of non-payment by the debtor. Under recourse factoring, the supplier retains all liability for non-payment of the invoice by debtors and so must repay advances issued by the third party financer in the event of non-payment by the debtor.

3. When factoring, the third party financer will normally inform the debtor that the trade debt has been assigned by the supplier. Therefore the assignment is a 'statutory assignment' and the financer is the financier is able to sue on the receivable in its own name, without involving the supplier, in the case of non-payment by the debtor.

Invoice Discounting

4. Invoice discounting occurs when the supplier assigns their trade receivables to a third party financer but the supplier retains responsibility for its sales ledger maintenance and all credit control collections – i.e. the third party financer acts simply as a lender and does not play a role in the relationship with the supplier's customers.

5. Under an invoice discounting arrangement, monies paid by the debtor to the supplier are paid directly into a trust account so that the financer has a more secure claim and access to monies paid. The assignment is an 'equitable assignment' and the financer is unable to enforce the assigned receivable in its own name and has to join the supplier to any enforcement proceedings against the debtor. The debtor is not necessarily informed of the assignment in this instance.

Invoice Trading

6. Recently, a new product has entered the market – invoice trading. Traditional factoring and invoice discounting involves the supplier (client) paying two charges – the discount rate (eg. 20p in each £1 advanced) which is charged on what is funding is actually used by the client (supplier), and a service fee which is typically the greater of a fixed charge or percentage of the supplier's turnover. So the client (supplier) must pay for the potential assignment of their entire loan book, as well as a discount rate on the funding actually utilised. Factoring is

more expensive than invoice financing due to the loan book management services offered. Non-recourse factoring is more expensive again due to the premium charged for the conferral of liability of non-payments to the financer.

7. Invoice trading allows suppliers to pay for invoice financing on an ‘invoice by invoice’ basis instead. Suppliers will select invoices from blue chip customers against which they wish to obtain financing. The platform will then pool a number of invoices due from a particular blue chip customer to a number of different suppliers, and then sell these assigned receivables to sophisticated investors as investment products. Suppliers are thus effectively offered invoice discounting, but on an ‘invoice by invoice’ pricing model.

<u>Supply Chain Financing</u>

8. Supply chain financing is a further form of invoice financing. Typically, the customer will establish an e-invoicing platform which will allow its suppliers to obtain invoice financing from a third party finance provider against an improved invoice due from that customer. This potentially reduces costs of financing as the third party financer will provide funding on the basis of the credit worthiness of the one customer, instead of factoring in the varying credit ratings of all the customers on the supplier’s loan book.

9. By its nature, this form of financing is fully disclosed – i.e. the customer has approved the assignment of trade receivables from the platform to the third party financer.

<u>Set Off</u>

10. Debtor's right to reduce the creditor's invoice by the amount the creditor owes to the debtor.

Annex B – Evidence collection methods:

1. To inform policy development and ensure that our analysis was based on the most robust evidence, the following evidence collection methods were undertaken:

    a. A online survey aimed at large firms for methodology
    b. an online survey distributed to Asset Based Finance Association (ABFA) members (see Annex A for the methodology);

c. face to face meetings with academic researchers, invoice financers, debtors, suppliers and business representative bodies.
d. Publicly available industry data.
e. International comparisons
f. Reviewing other IAs within this area

Survey of ABFA members

Sampling approach

2. The survey was sent ABFA who distributed to their members. ABFA have 31 UK based (including Northern Ireland) members with another 3 Republic of Ireland members. Therefore, potentially 3 respondents from Northern Ireland could have responded to the questionnaire however we are unable to identify or filter these responses out.

Research Methodology

3. The survey consisted of multiple choice questions, open ended questions and ratio scale questions. The survey was split into different sections asking a number of questions on factoring, invoice discounting, the potential costs of introducing new regulations to nullify bans on assignment of trade receivables and some general questions about their organisation.

4. The survey ran for just over two weeks from the 8th August to the 26th August 2014.

5. We received 20 valid responses (10 responses were removed because the vast majority of questions were unanswered). Of the 20 valid responses, some questions were left unanswered by some respondents and not all questions were asked to all respondents.

Online Survey aimed at large firms

Sampling approach

6. The Pilot survey was sent to 14 organisations known to BIS within the Prompt Payment policy area. The sample for the final survey was compiled using the FAME company database (as it can be used to identify large companies using the Company Act 2006 definition) and BIS connect (an online tool that stores information about the Department's stakeholders and their contact details). In addition we also asked the Chartered Institute of Purchasing and Supply (CIPS) and the Association of Corporate Treasurers (ACT) to distribute the link to their networks using their Linked-in profile.

7. Therefore, as stated previously in the IA the Survey is not a representative sample of firms potentially in scope of the policy options.

Research Methodology

8. The survey mostly consisted of multiple choice questions but also included some interval scale questions and a limited amount of open ended questions.

9. The survey mostly asked questions on the prompt payment report policy however it did contain a couple of questions regarding Ban on assignments. This is because, from early discussions it seemed ban on assignment were not widely known about.

10. Before launching the full survey BIS conducted a pilot. This allowed us to test people's understanding of the language used and to test the overall flow of the questionnaire and to make the necessary changes were needed before sending out the survey to the wider sample. As a result of the pilot we modified one question which respondents had found difficult to interpret. This meant that for this particular question we were unable to merge the results from the pilot and the final survey results. Other minor changes were made such as an addition of a comment box which did not invalidate responses made in the pilot.

11. The pilot survey ran from the 10th July to 4th August and the final survey ran for around two weeks; from the 28th July 2014 to 12th August 2014.

12. We received 35 valid responses (29 responses were removed because the majority of questions were unanswered), 7 were from the pilot and the remaining 28 responses were from the final survey. Of the 35 valid responses, some questions were left unanswered, not all questions were asked to all respondents and as mentioned before one question changed significantly between the pilot and final survey, hence pilot responses for that question was invalid.

International Comparisons

13. International comparisons were also limited. We engaged and researched ban on assignment measures in several countries including the US, Canada, Australia, Germany and France. There were very few datasets and only one concrete assurance from Australia that the effect of ban on assignment clauses would be reviewed in December 2014 with a final report due in January 2015.

Impact Assessments

14. We reviewed the Final Impact Assessment for banning exclusivity clauses in zero hour contracts, July 2014, IA number BISLMD002 to learn from methodology used to assess the policy and to identify lessons learnt.