Forum of Private Business

The business people – an extension to your team

Referendum 207 report

April 2014

Summary

Late payment

- Late payment appears to have increased over the last year. 23% of businesses report an increase in contract payment whilst 3% report a decrease. 29% have seen an increase in the average number of days beyond the deadline that a payment is made late whilst 8% reported a decrease. 19% have seen an increase in both elements of late payment.
- The improving economic situation however means the number of businesses seeing late payment as a serious problem has been static according to the SME finance monitor[(1)].
- 39% would like to see prompt payment better promoted, 37% would like to pay VAT on money that has entered their account rather than when an invoice is submitted and 36% wanted to see persistent late payers barred from government contacts.

Banking services

- 59% of businesses review their banking services annually, 13% every few years, 7% on renewal of products and 21% would only review their service if there was a problem.
- Bank charges and reduction/calling in of loans or overdrafts were the most harmful activities undertaken by the banks, whilst access to finance was also harmful to those looking to survive or grow using external finance.
- Comments were mainly negative with the impact on business growth caused by an inflexible attitude to finance for growth and a reduction of margins.
- 11% felt that their bank offered excellent value for money, 43% good value for money and 32% average value for money. 14% felt it offered poor or very poor value.
- The cost of banking services (69%), poor customer service (66%) and unexpected charge increases (57%) were then main reasons businesses may consider switching.

Alternative finance

- Just 18% would consider an alternative provider to replace their current banking services, 13% would consider them for some or all of their current financial problems and 14% would consider them for new or additional finance.
- 26% would not consider an alternative provider and 30% were uncertain.
- The main barriers for newer providers were cost (35%), awareness (21%) and lack of reliable advice (19%). Almost 1 in 4 were concerned that looking at alternative providers may impact on their current banking products.

Changes needed to finance a sustainable recovery

- 15% wanted more flexibility/less centralisation in lending, allowing bank managers to make choices based on individual need rather than generic assessments. 14% felt that there needed to be greater access to finance, 13% wanted less red tape from banks and 12% wanted banks to shoulder a greater proportion of risk.
- 10% wanted greater support for cash flow issues – 6% through enforcement of the late payment charges and 5% in other ways.
- 9% wanted greater incentivisation through the tax system, with VAT and corporation tax the most frequently mentioned areas that could be incentivised for businesses.

Recommendations

Late payment

Re-introduce a statutory reporting requirement for large companies on payment practice

The Department for Business, Innovation and Skill's discussion paper on late payment was welcome and contains a range of proposals, including a voluntary reporting requirement for companies on late payment. This would replace a previous statutory requirement that was removed last year. In order to be successful, any new (voluntary or mandatory) requirement must ensure that the presentation of the data is done in a transparent – and if possible – standardised format. Secondly, reporting should include whether the company operates a supply chain finance scheme for suppliers and the extent to which it was used during the previous year.

Clarification and support around enforcement of the EU Late Payment Directive

Article 7 of the 2011 EU Directive on Late Payment suggests that business representation bodies can represent their members in challenging unfair payment practices. The Forum of Private Business would like certainty from government around what adequate and effective means may exist to support this process in the UK – an obligation for a Member State in the Directive. Thereafter, groups can be brought together to ensure costs are shared in creating case law around the term 'grossly unfair'.

Banking services

Revisit the idea of shared bank branch services

Competition is partly driven by access in the banking sector. This is increasingly limited by a reducing branch network that continues to decline. This is sometimes cited as a barrier by would-be banking entrants to the market. Branch sharing can take one of two, or both, options. Inter Bank Agency Agreements facilitates use of a local bank's counter by small business customers of other banks. Neutral Shared Branching means any branch can provide basic counter and related services, to agreed operating standards, delivered by a third party provider(s) on behalf of participating banks.

Support banks to create portable credit histories for small businesses

The consultation on credit data sharing has recently closed but the Treasury is looking at how more information can be shared between the banks and credit reference agencies, to ensure businesses can access a wider variety of finance options. Opening up credit data will increase the reliability of credit scoring and therefore allow alternative lenders to make more informed decisions about whether or not to lend to a business. However, the process of sharing SME credit data with just intermediaries of credit reference agencies is a missed opportunity. There is no practical reason why large banks cannot provide customers with online portals where they can share a 'portable credit history' with whoever they like, whether bank, lender or supplier. Making this happen could have a fast and dramatic effect on SME credit availability. Not only would this place the power in the borrower's hands, not the CRAs, but the technology already exists.

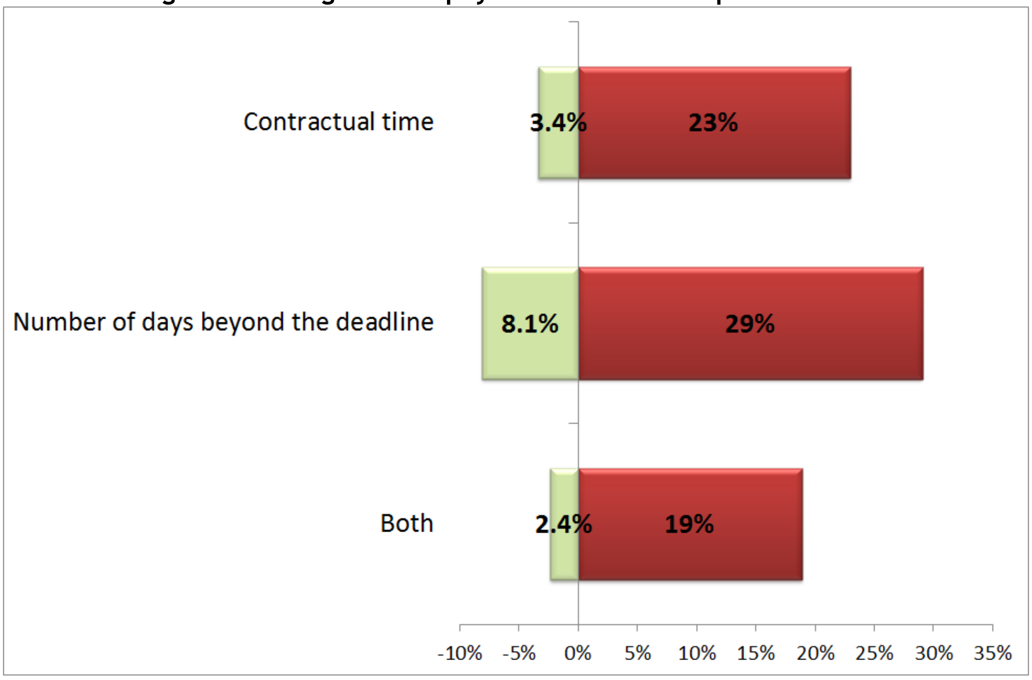
Late payment

Late payment is an ongoing concern for small businesses. The most recent Late Payment Index from Experian was published in Q3 2013 and indicates a slight quarterly rise. Experian reported that UK businesses paid their overdue bills between July and September 25 days late on average, compared to 24.6 days in the second quarter. (2)

Bacs estimated that the national late payment debt now stood at £30.2 billion in April 2013, with the average business waiting for £31,000 in overdue payments. A new report due shortly will show how this has changed in better economic conditions. (3)

We asked business owners whether the contractual time in which customers pay had increased, whether the average number of days beyond the contract payment deadline had increased, or whether both had increased, in 2013.

Figure 1: Change in late payment in 2014 compared to 2013

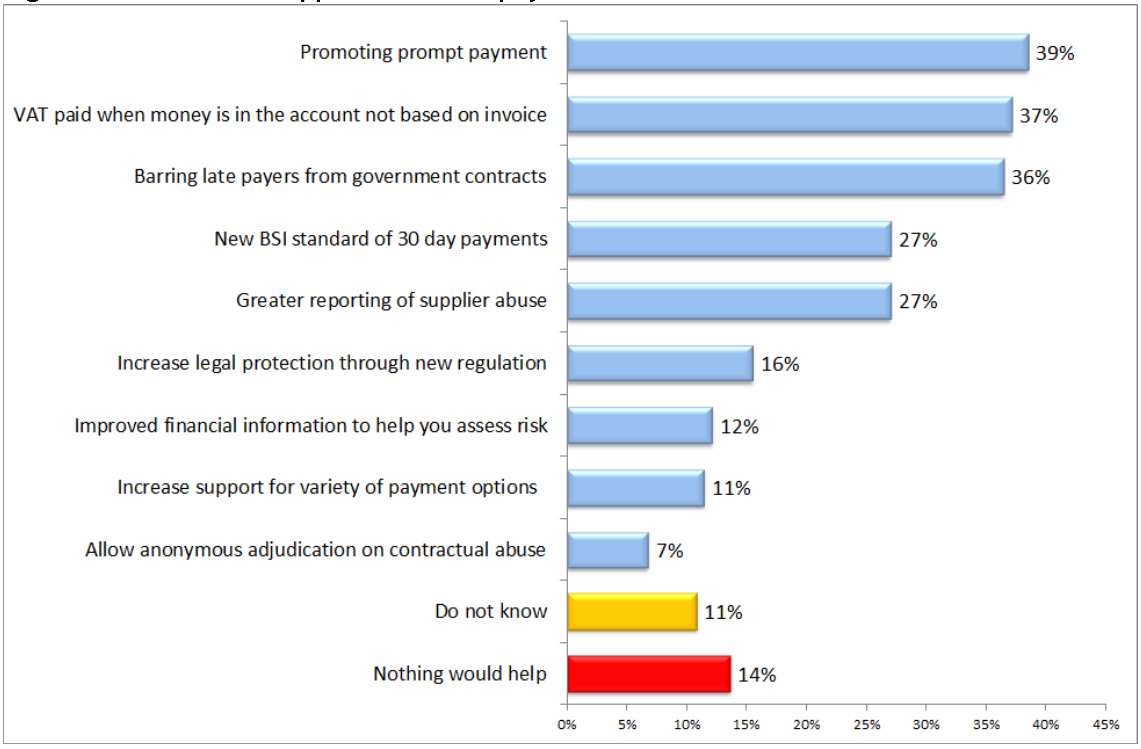


Some businesses do not differentiate between the contractual time in which customers pay and the number of days beyond the contract date in which the client pays, this can be because the company asks for immediate payment or because they work on the basis of the number of payment days from the day at which they submit the invoice. Nevertheless, the results show that contractual times and late payment have mostly increased, rather than decreased, for Forum members.

According to Hilton Baird, businesses with a turnover of between £500,000 and £3 million – the typical size of Forum members' businesses – are experiencing the longest delays in payment terms and the overall payment gap has increased, although credit terms (typical contract time) had improved slightly. More worryingly, the impact of late payment appears to have increased with 9% of businesses reporting they had to turn away new work and the number of businesses who had to increase the time spent on chasing invoices, increase borrowing or pay their suppliers later going up. (4)

Overall, late payment remains a significant issue for about 1 in 10 businesses, sometimes exacerbated by lack of external finance. Presently, only a minority of businesses try to charge interest on late payment as they are entitled to do under the 1998 Late Payment Act, mainly because customers would ignore it or there is the potential risk of losing customers. (4)

Figure 2: Government approach to late payment



39% of businesses want greater support for the promotion of prompt payment, rather like the ICM prompt payment code. This has not really been pushed for a number of years and there appears to be no real reason for companies to sign up to it or abide by some of the principles.

One way in which this could change is if persistent late payers were barred from government contracts, an idea supported by 36% of respondents and felt to be more effective than naming and shaming companies where government money is concerned. It also fits in with 'nudging' companies towards ethical practice.

37% would like HMRC to show more leniency, so that VAT could be paid based on when the money is in a business account rather than when invoices are submitted. In 2013 Hilton Baird saw a significant drop in the proportion of businesses admitting that they have had to pay HMRC late as a consequence of late payment, otherwise this figure may have been higher. The fact remains however that while 64% of businesses have a credit balance of under £5,000 there is a potential for serious cash flow indications if a large payment is delayed.

27% would support a new BSI standard for 30 day payments and the same percentage would support wider use of the Forum's Hall of Shame (and similar websites) to report supplier abuse.

Just 16% wanted new regulations to increase legal protection with 14% preferring that nothing is done. 12% felt that improved financial information would help them assess risk as business owners felt that the combination of formal and informal methods they currently use to assess risk was quite effective.

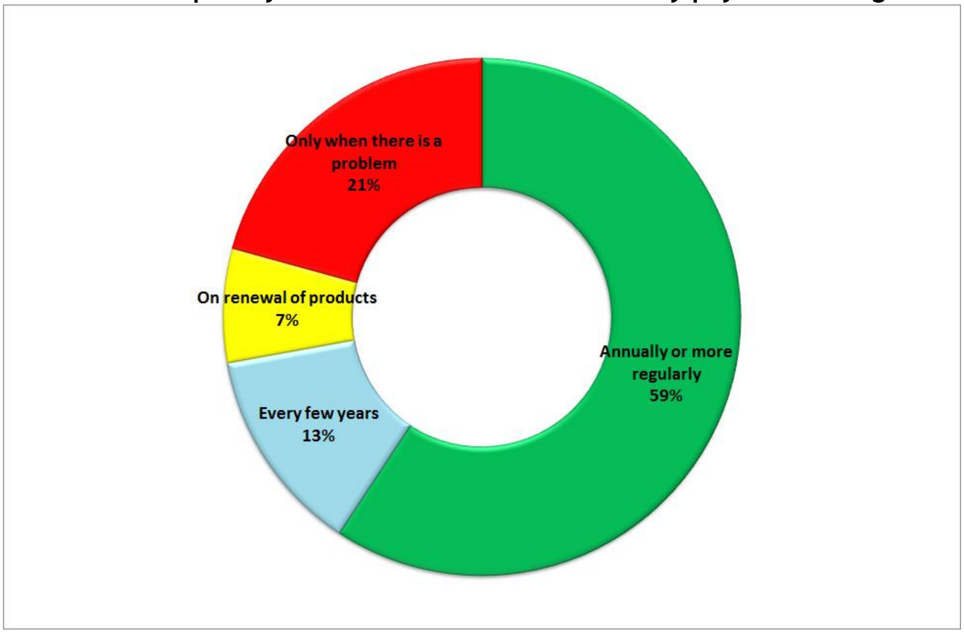
11% wanted greater support for using a variety of payment options so that businesses can pay in a number of ways. With the Payments Council shortly launched PayM businesses will shortly be able to pay by phone number, which should help address this issue. 7% of businesses wanted anonymous adjudication on contractual abuse as businesses. The low numbers supporting this proposal are down to uncertainty as to how it would work in practice. With similar supplier abuse protection in place in the grocery sector, understanding how the process works there will be vital for confidence in such schemes.

Bank services

"Banks like secure companies; prove you're secure and financially competent and get the manager on your side, then they treat you as a positive asset." ***Member comment***

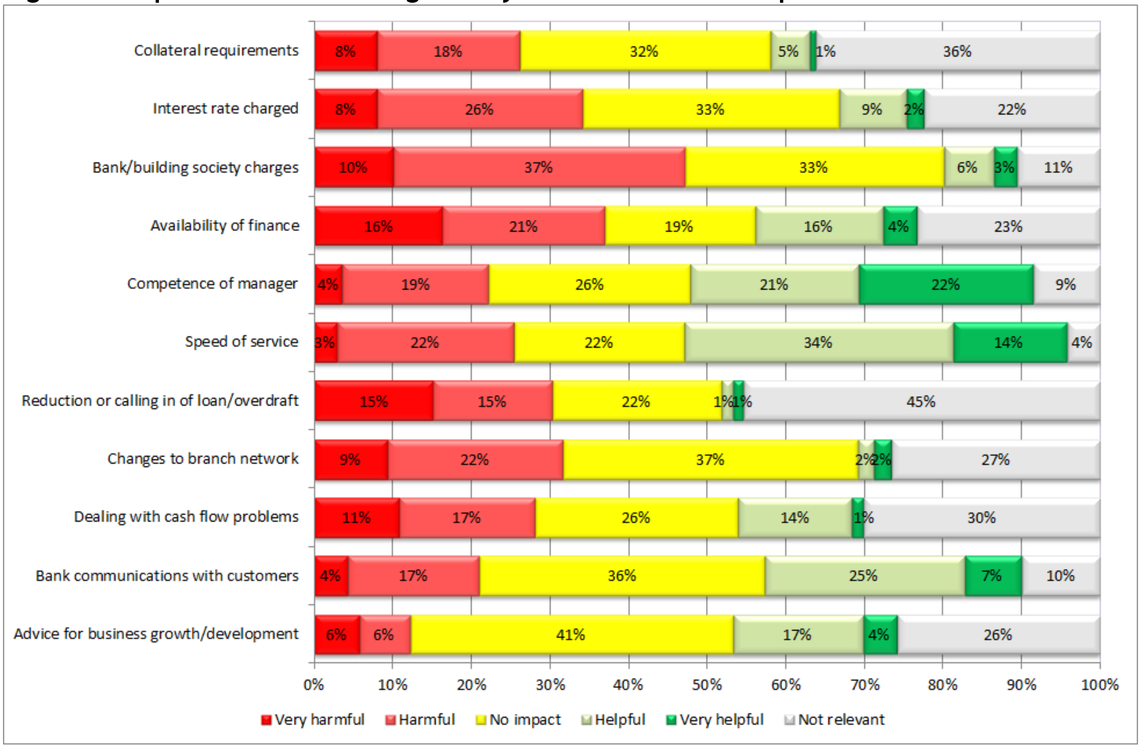
We asked businesses how often they reviewed their bank services. Three in five reported that they did so on at least an annual basis. 21% only reviewed their relationship with the bank when there was a particular problem and 7% looked at their banking relationship only when it came to renewing their main financial products.

Figure 3: How frequently businesses review the cost they pay for banking services



With many businesses wanting to grow in 2014, the Forum also wanted to understand business' view of how banks could support them to do so.

Figure 4: Impact of bank/building society attitude to business performance



As can be seen from Figure 4, charges from banks and building societies, together with the availability of finance, are the main issues. In contract business advice, communications and the managerial competence are seen as positive elements of bank intervention.

“Banks are increasing their margins and charges. This has increased our costs. Banks (and other suppliers) see small businesses as a cash cow.” ***Member comment***

Many of these questions have been asked in the past as part of the Forum’s bank survey. This Referendum report response largely confirms the changes noticed since 2006 and the level of suspicion that businesses have when it comes to the banking culture, though the feedback on local bank managers is relatively positive in comparison.

In this report we added in bank communications and in 2013 added in changes to the branch network, dealing with cash flow problems and advice for business growth to reflect branch rationalisation, reductions of overdrafts to limit banking liability and more positively the mentoring programme.

Any score of less than 3 suggests that the banks are more likely to be helpful than harmful whilst scores over 3 indicate that the actions of the banks are still viewed as more harmful than helpful.

Figure 5: Comparison over time of the impact of bank/building society attitude

	2014	2013	2006	2004	2002
Collateral requirements	3.3	3.2	2.88	2.86	2.99
Interest rate charged	3.3	3.1	3.09	3.06	3.18
Bank/building society charges	3.5	3.6	3.23	3.25	3.3
Availability of finance	3.3	3.3	2.43	2.5	2.69
Competence of manager	2.6	2.8	2.35	2.29	2.47
Speed of service	2.7	2.7	2.39	2.32	2.45
Reduction or calling in of loan/overdraft	3.4	3.5	3.16	3.22	3.44
Changes to their branch network	3.3	3.3	n/a	n/a	n/a
Dealing with cash flow problems	3.2	3.3	n/a	n/a	n/a
Bank communications	2.9	n/a	n/a	n/a	n/a
Advice for business growth/development	2.9	2.9	n/a	n/a	n/a

Aside from the interest rate charged seen as deteriorating slightly, together with the collateral requirements required, the indicators suggested a marginal improvement in how banks treat businesses and broadly no real difference to 2013.

The feedback from businesses on the impact of the banks and financial institutions can be compared to what the data collected on business banking as part of the SME finance monitor:

- Over the last year collateral requirements have dropped for loans but increased for overdrafts.
- Interest rates have not really changed for loans and increased marginally for overdrafts, however the concern for members is the gap between the amount paid and the Bank of England base rate.
- Bank charges, charges for loans and overdrafts have remained the same over the last year, these have however become marginally more affordable, although still detrimental to businesses.
- Success rates for core banking products have not changed over the last year.

Impact of banking services on businesses

"I'm having to turn down export work because the bank won't lend against a letter of credit - then complains I don't turn over enough and don't make sufficient profit according to their computerised credit checker." ***Member comment***

Most comments about the impact of banking services were simply that they have had little or no impact and businesses have generally adapted to the new banking climate. In total 42% of those that gave a response indicated that this was the case.

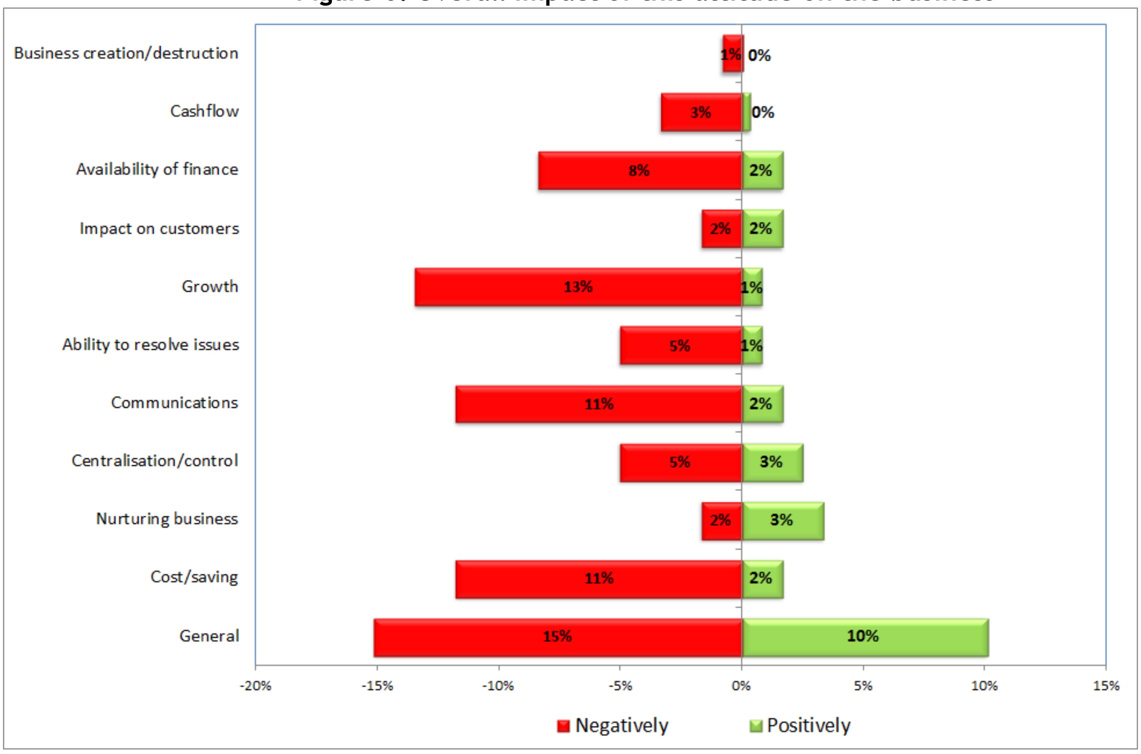
"Online banking system supplied by bank incompatible with latest Microsoft products and no communication alluding to this fault at all." ***Member comment***

Most of the comments are negative as can be seen from Figure 6 below, however the majority of issues were to do with bank charges or communication issues, where the most serious concern from a small number of business owners was that the bank delayed making a decision on finance until the business opportunity had passed. Conflicting information was also an issue, although the most common gripe was the lack of communication on key issues. Online banking systems were mentioned by a small number of organisations with one hotel stating that although their bank did offer good value for money, the online system was causing them to consider changing.

"Our NatWest Business Manager understands our business fully." ***Member comment***

1 in 4 comments were positive, with 3% feeling that the bank was actively nurturing their business and supporting their development. A further 10% replied that the bank had generally been positive in the way they engaged with the business.

Figure 6: Overall impact of this attitude on the business



Holding back growth was the key way in which businesses felt that banks had impacted negatively on their business, either by rejecting funding, not offering the amount needed to grow or not supporting them in pursuing opportunities to export.

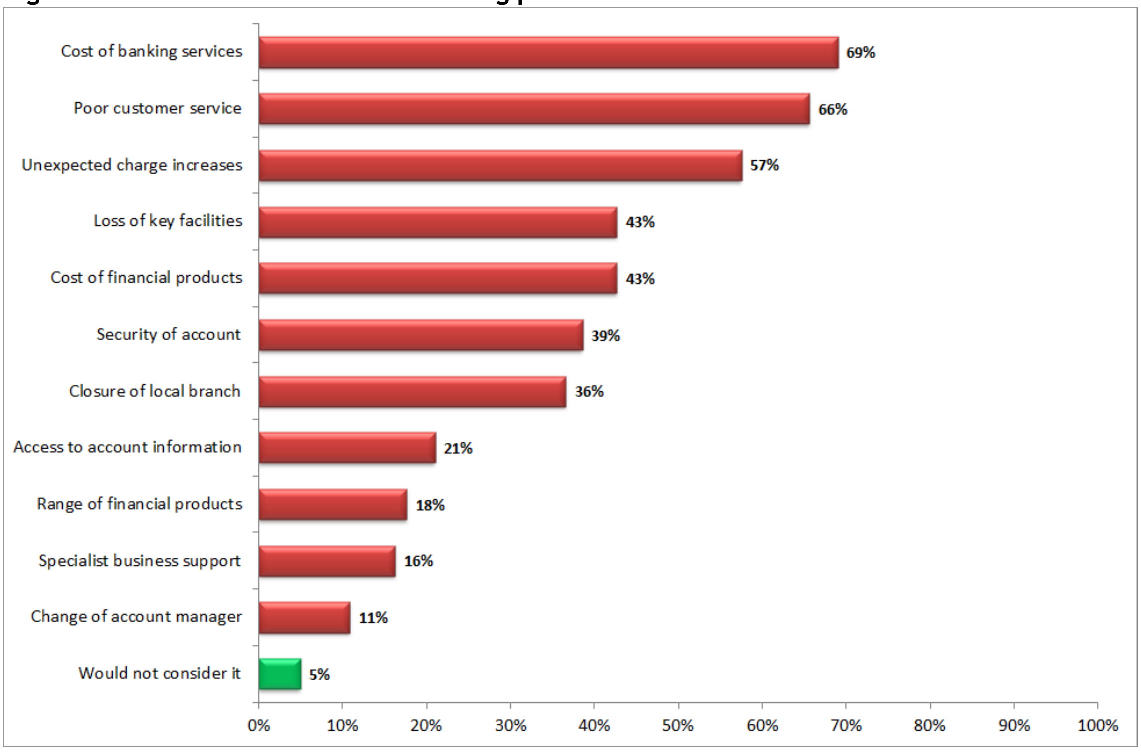
The impact of the availability of finance was linked to growth opportunities and was again seen as negative although a number of individuals did report that they had new or extended overdraft facilities offered to them by their bank. In most cases businesses reported refusal of loans as the reason for this view.

Switching provider

Two thirds would change banks if they received poor customer service or felt that the cost of banking services were excessive. A majority would also consider leaving their current provider if there were unexpected charge increases. Just 5% would not consider switching banks if they had been treated badly or the performance of the bank was inadequate.

Closure of the local branch was industry dependent and the security of the account was an issue for 39%, surprisingly low for what was expected to be a key reason for leaving their current supplier. The cost of financial products and access to key facilities were mentioned by 43%.

Figure 7: Potential reasons for switching provider



Research done by the Forum alongside the OFT inquiry into bank switching indicated that the main motivations for switching provider were a better service at the new bank (26%) or a poor relationship with the previous bank or its staff (30%). Costs of banking, either through access to free banking (22%) or lower prices (19%), were the second main reason for switching, along with a refusal of their previous bank to provide credit (21%).

The research also indicated that procrastination (30%), the hassle of switching (33%) and the perception it would not make much difference (23%) were more likely to be reasons for staying with the same bank rather than an existing good relationship (21%).

Cross referencing the potential reasons for switching with whether businesses feel that their bank is helping or harming them is shown in Figure 8.

Of those that gave poor customer service as a reason why they would switch, 52% felt that their bank offered good or very good value for money, while 15% felt that it offered poor or very poor value for money. This provides a good example of how people who experience extremes in service levels are more likely to have cited this as a reason for switching.

Customer service was one of the main reasons for staying with their current provider so this may be why relatively few businesses are looking to switch despite expressed concerns. For this reason the figures in Figure 8 are thought to be volatile, for instance businesses who lost their local branch would be more likely to consider this to be a reason for switching in the future and a security breach would make this issue more likely to be considered as a reason for switching.

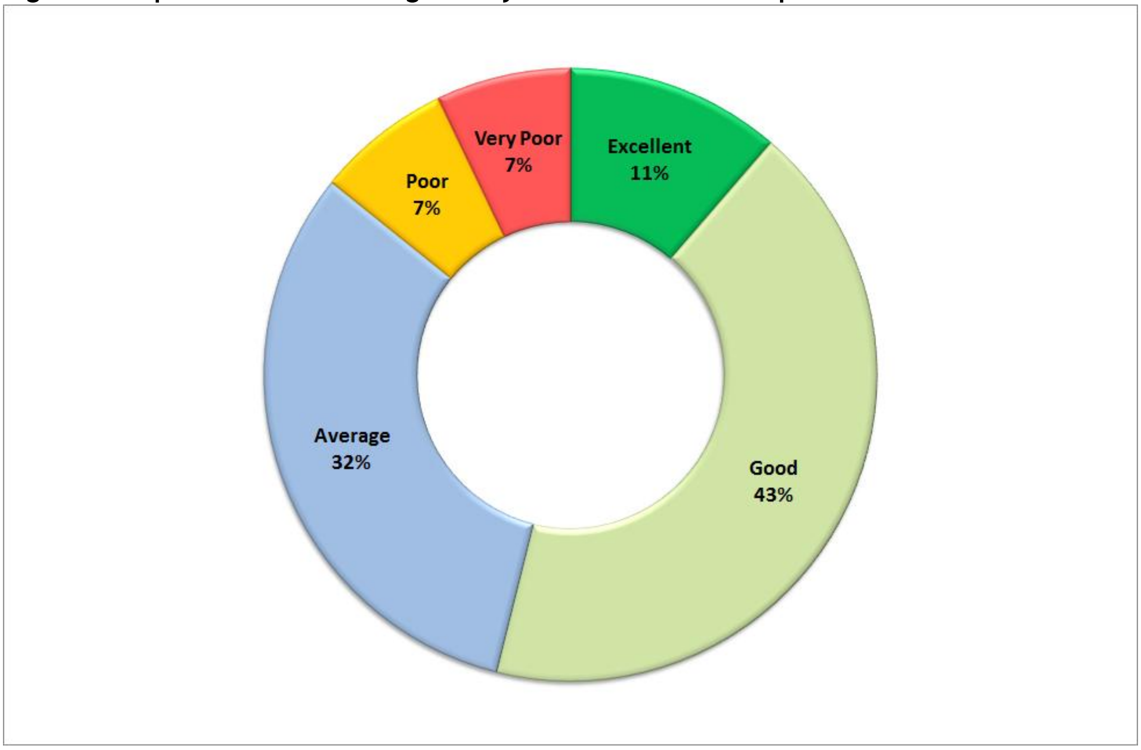
Figure 8: Impact of the attitude of the bank on likelihood to switch

Potential reason for switching	Indicator	Positive	Negative
Poor customer service	Overall value for money	52%	15%
Closure of local branch	Changes to the branch network	2%	37%
Range of financial products	Availability of finance	3%	72%
Cost of financial products	Interest rate charged	13%	44%
Security of account	n/a	n/a	n/a
Access to account information	Bank communications	27%	29%
Loss of key facilities	Reduction or calling in of loan/overdraft	2%	35%
Cost of banking services	Bank/building services charges	9%	51%
Unexpected charge increases	Bank/building services charges	8%	54%
Specialist business support	Advice for business growth	25%	33%
Change of account manager	Competence of manager	44%	38%

Value for money

The Forum asked members to rate the value for money they thought their bank offered, chosen as a measure given cost is a key driver for competition in the small business account market.

Figure 9: Impact of bank/building society attitude to business performance



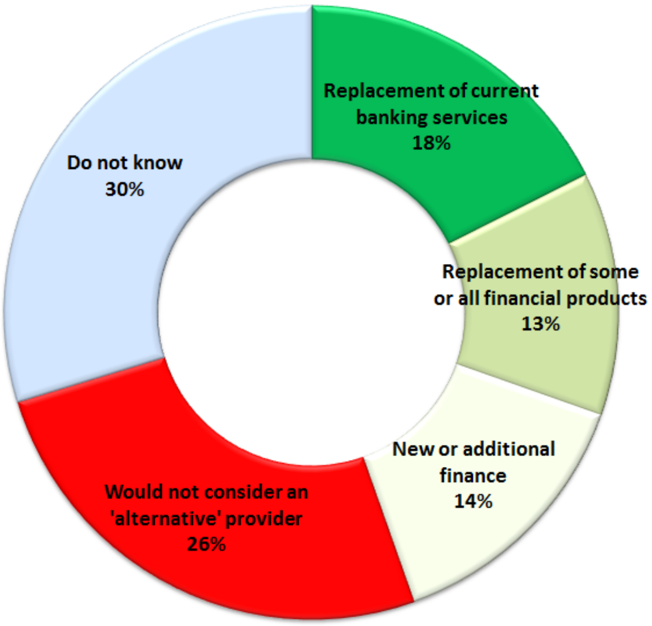
Overall 54% consider the value for money they receive from their bank to be good or excellent, while a further 32% feel that there is little difference between banking brands or are broadly satisfied. 14% reported that they felt the value for money they received from their bank was poor or very poor, which is quite similar to the figures from members in 2008/9.

With the ‘Switch Guarantee’ introduced in 2013, the 46% of businesses who are not happy with their account costs have an opportunity to change providers.

Alternative finance

The difficulty that challenger banks face is highlighted by the chart below. Just 18% would consider using an 'alternative' provider (in the sense of a non-high-street bank) to replace their current banking services.

Figure 10: When business owners consider a newer provider of banking services/finance



"Supply chain finance and impact of crowd funding needs full investigation." ***Member Comment***

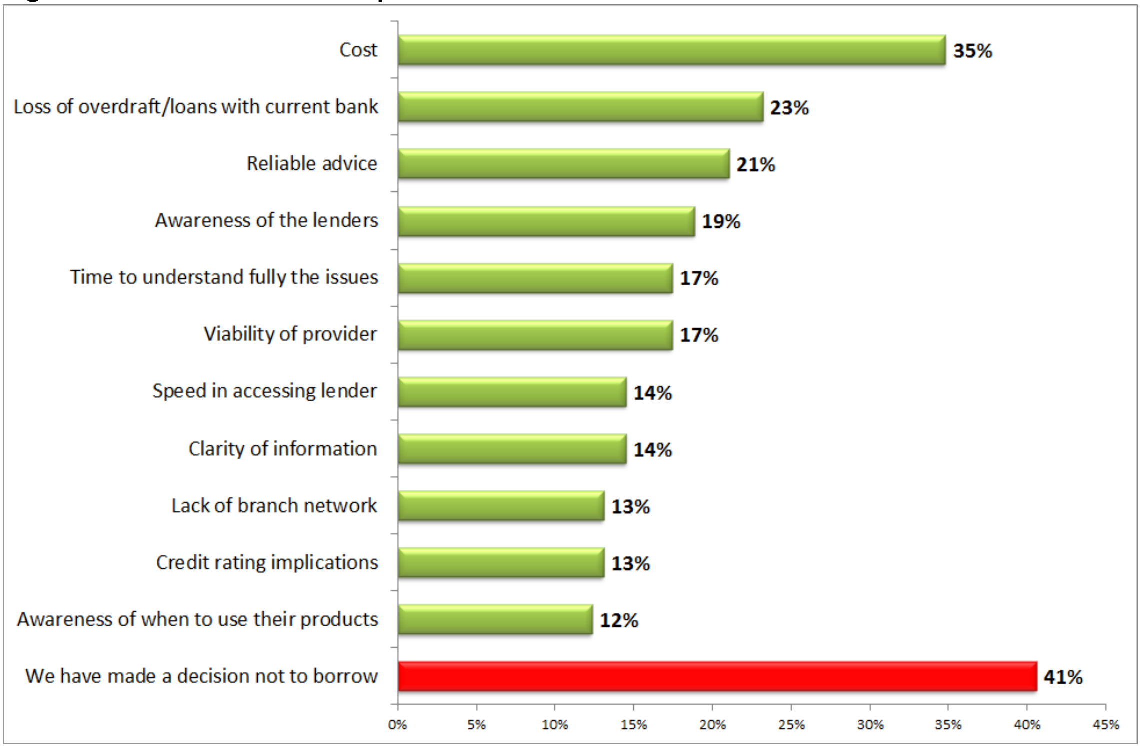
13% would consider an alternative provider for some or all of their financial products and a similar number would consider them only for new or additional finance. 26% would not consider alternative providers at all and 30% did not know, with some feeling there was not enough information available, or were suspicious of new types of funding. In the case of supply chain finance, some larger businesses have used this as a way of introducing invoice discounting or letting their suppliers take more of the risk.

Cost was the main barrier to businesses considering alternative providers, with businesses perceiving providers could not be competitive price wise. In 2009 36% reported that cost was the major issue that they had with finance providers (traditional and alternative) so in some ways this is not an issue that only affects alternative finance providers.

Loss of current credit lines was also an issue, with almost a quarter reporting this, whilst one in five were also concerned about the lack of reliable advice. Time to understand the issues, the viability of new providers and a lack of awareness of providers in the market place are also significant issues as business owners see it as a time efficient process to focus on the traditional banking sector.

Overall 41% would not consider alternative financial providers as they are simply looking to fund themselves – this corresponds closely to the 41% of permanent non-borrowers indicated in the corresponding SME finance monitor.

Figure 11: Barriers for newer providers of finance



The reasons why businesses are reluctant vary slightly according to their general attitude to alternative provision. Loss of current credit lines are the main concerns for those considering replacement of current banking services, as there are concerns as to whether alternative providers would be able to offer similar financial products and the replacement of some or all of their financial products. In both cases cost was the second major reason.

Figure 12: Most common barriers based on business owner's willingness to consider them

	Overall	**Replacement of current banking services**	**Replacement of some / all financial products**	**New or additional finance**	**Would not consider an 'alternative' provider**
Primary reason	A decision made not to borrow	Loss of lending with current bank	Loss of lending from current bank	Cost	A decision made not to borrow
Second reason	Cost	Cost	Cost	Awareness of the lenders	Cost
Third reason	Loss of lending with current bank	A decision made not to borrow	Awareness of when to use their products Time to understand fully the issues	Loss of lending from current bank Viability of provider	

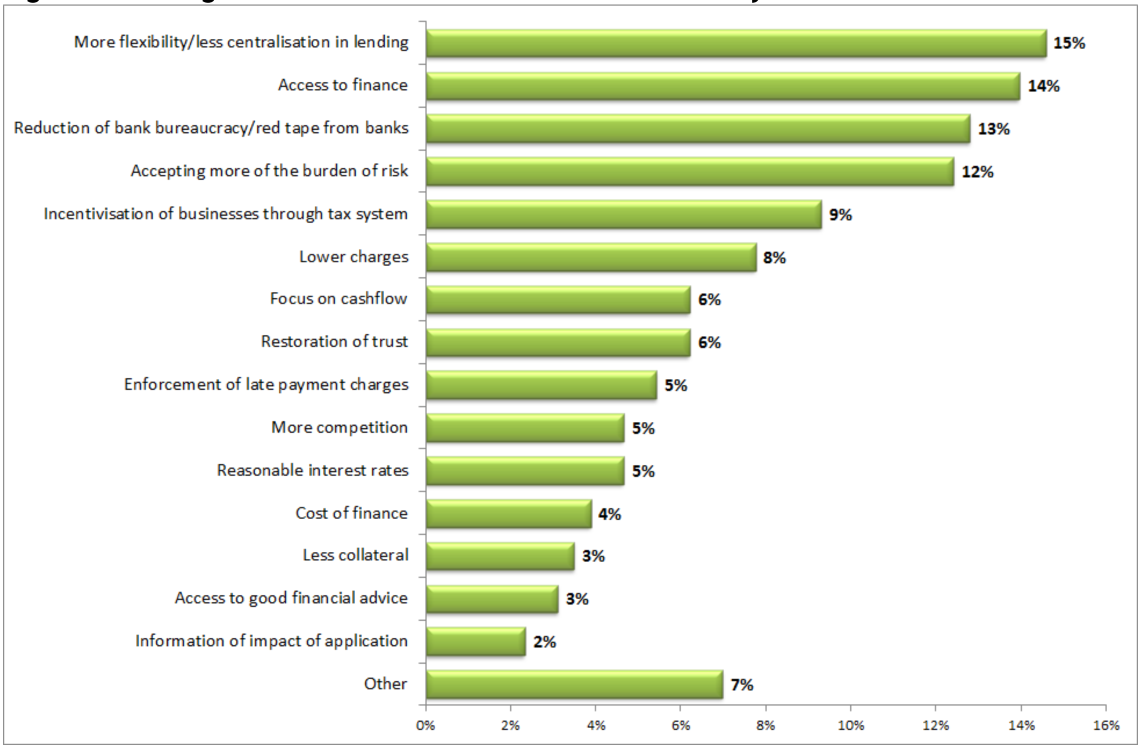
Cost was the primary barrier for new or additional finance with an awareness of lenders also important. There is a perception that alternative providers only offer equity, invoice or other asset-based finance and businesses would need to know what else was out there. This may also indicate a reluctance to consider a commercial financial broker.

Changes needed to finance a sustainable recovery

"For the main banks to return to empowered local managers, as per the Handelsbanken model." ***Member comment***

The main change that businesses wanted to see was more flexibility in cost, bureaucracy and access to products from banks when considering lending applications. Businesses wanted to be treated on an individual basis rather than being put into generic risk categories. There is a belief that bank managers want to help but are restricted by their own organisation rather than lacking the skills or ability themselves. These issues were raised by around 1 in 5 businesses, with 15% highlighting the over centralisation or lack of flexibility in the system and 13% wanting a reduction in red tape from the banks.

Figure 13: Changes wanted to finance a sustainable recovery



14% wanted to see an improvement in access to finance, particularly finance for growth and development. 12% wanted the banks to shoulder a greater burden of risk as they seemed reluctant to agree to fund the opportunities that business owners can see in the marketplace.

9% wanted greater incentivisation through the tax system though polling was before the 2014 Budget when the annual investment allowance was doubled. Most businesses were more concerned with cash flow implications of a 20% VAT rate, Corporation tax and Employers NI.

Cost of finance is always an issue with 4% stating that the general cost of finance was an issue. 8% wanted lower bank charges, 5% wanted more reasonable interest rates and 3% also wanted banks to seek less collateral. In addition 5% wanted to see more. 1 in 10 businesses focussed on cash flow, with greater enforcement of late payment charges to create a culture of prompt payment being indicated by 5% of business owners.

(1) BDRC, SME Finance Monitor Q4 2013, February 2014
(2) Experian, "New Rules on Late Payment", July 2013
(3) Bacs, Cost of late payment research, April 2013
(4) Hilton Baird, Late Payment Research, January 2014

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