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Hidden Benefits of Corporate Finance Come Under Spotlight

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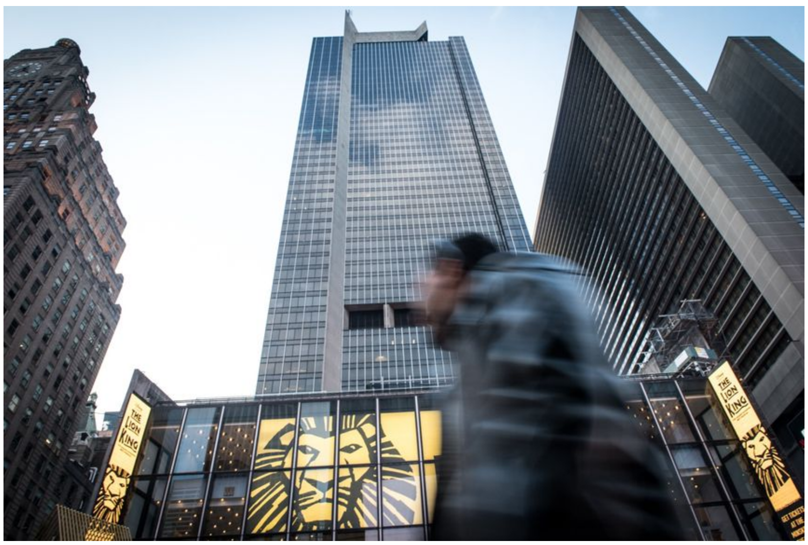

By Julie Steinberg

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Big businesses are pushing hard to wring profits out of the smaller companies that supply them with goods and services. One type of deal, known as a supply-chain finance rebate, has come under the spotlight of accounting groups for obscuring who benefits most from the arrangements and whether that masks true financial risk.

Supply-chain finance has quietly grown into an important piece of financial plumbing, helping businesses stretch the amount of time they have to pay their suppliers.

Supply-chain finance deal volumes totaled $1.8 trillion in 2021, up 38% from a year earlier, according to BCR Publishing, which tracks the industry. A subset of those deals—the number is unknown because deals are private—offers rebates to the big businesses who participate in the programs.

The Financial Accounting Standards Board and the International Accounting Standards Board, which set accounting standards, have been working on new disclosure requirements for companies with supply-chain finance programs.

The FASB on Wednesday approved a rule requiring companies to disclose the key terms and size of their programs. While the rule doesn't explicitly mention rebates, companies that get them from their supply-chain finance providers would be expected to disclose them, said a FASB spokesperson.

Some, including investors in supply-chain finance deals such as Connecticut-based Fermat Capital Management LLC, have been pressing the accounting bodies to include rebates as part of the disclosures.

Supply-chain finance programs are often presented as win-win for companies—or buyers, as they are known—and their suppliers, but suppliers might not know the buyers sometimes directly profit from these arrangements by getting rebates.

"The supply-chain financier is sharing the benefit with the buyer, so it becomes a problematic secret commission," said Dean Paatsch, co-founder of Ownership Matters, an Australian accounting and governance advisory firm. He calls the payments a "sugar hit" to companies' cash flows and margins and recommended to the IASB that companies disclose any financial benefits they receive from supply-chain finance providers.

Some say rebates are a potential conflict of interest because companies eager for cash they generate might pressure suppliers to join their supply-chain finance programs. Critics say rebates add to suppliers' costs, where they are drawn from, and flatter buyers' income statements.

Supply-chain finance works like this: A financial institution, often a bank, pays a company's suppliers faster than normal payment terms, which can range from 60 to 120 days. The supplier agrees to receive slightly less than it would get by waiting and pays the bank a fee. The company pays back the bank the full amount down the road. The bank keeps the difference as profit.

A rebate funnels some of that profit back to the company. Suppose Company A owes Supplier B $100. Supplier B elects to get paid early at a discount, and accepts $98 from the bank that arranged the program. The bank splits the $2 with Company A.

Another concern with supply-chain finance deals is that they are classified as accounts payable on balance sheets, rather than debt. They are both liabilities, but many key measures of leverage used by banks to measure a company's ability to pay rely on the debt calculation.

If a rebate is used, companies are supposed to count the programs as debt. Some banks are wary of financing programs with rebates unless the client agrees to classify the deals as such.

Not everyone thinks they are controversial. Dave Skirzenski, chief executive of Raistone Financial Corp., a trade finance firm, says he doesn't believe supply-chain finance rebates should trigger accounting treatment different from the rebates companies get from using certain corporate credit cards. Mr. Skirzenski says supply-chain finance programs should be disclosed, but that investors should use them as a jumping-off point to ask companies about specifics like rebates.

Last year, Paramount Global, formerly ViacomCBS, explored a supply-chain finance program with Wall Street banks, according to people familiar with the potential deal. Matrix Private Capital Group, the firm founded by Dick Fuld, the former chief executive of Lehman Brothers Holdings Inc., had suggested a rebate. Citigroup Inc. and JPMorgan Chase & Co. were uncomfortable with the idea, some of the people said.

Paramount was also uncomfortable with the idea and didn't move forward with that structure, some of the people said.

Rebates can sometimes come in the guise of data-access or marketing fees. As long as money is remitted to the company, it counts as a rebate, industry participants say.

Taulia, a supply-chain technology platform and a unit of German software giant SAP SE, extended about $8.7 million in so-called information-access fees to companies for its fiscal year 2021, on revenues of around $50 million, according to financial documents viewed by *The Wall Street Journal*.

"The aim of supply-chain finance programs is to provide suppliers with choice and flexibility when it comes to when and how they are paid," a Taulia spokesperson said. "Fees for the buyer seek to offset their costs and efforts to run a program."

She said the firm welcomes transparency and clarity that updated accounting standards will bring. She said Taulia's information-access fees for fiscal year 2022 dropped to $2.3 million, on revenues of more than $60 million.

Much of the industry shuns rebates, said Rudolf Leuschner, director of the master of supply-chain management program at Rutgers Business School. The industry relies on a 2004 U.S. Securities and Exchange Commission speech as the seminal guide to best practices. Bankers and accountants typically interpret the speech as advising against rebates or financial incentives.

Home-improvement company Masco Corp. in 2019 told the SEC it had negotiated a marketing fee with its suppliers, which created “a presence of economics sharing and could be viewed as a debt-like characteristic,” according to securities filings. The company said that though the marketing fee was “inconsequential,” it would stop the practice.

British telecom Vodafone Group PLC also made money off its supply chain. It put money into a fund that invested in supply-chain finance assets, including those tied to Vodafone, that were sourced by Greensill Capital, a specialty lending firm that collapsed last year. Vodafone made a return from the fund, said people familiar with the program.

A Vodafone spokesperson said the company redeemed its holdings in the fund in 2019 and hasn’t invested in similar funds since.

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