

<b>Institution: University of Leeds</b>
<b>Unit of Assessment: C19 Business and Management Studies</b>
<b>Title of case study: CREDIT MANAGEMENT RESEARCH CENTRE (CMRC): Improving credit management practice, influencing policy and enabling knowledge transfer</b>
<p><b>1. Summary of the impact</b></p> <p>The ability of companies and organisations to pay and recover debts affects and reflects the financial health of UK PLC. Research by the Credit Management Research Centre (CMRC) led by Professor <b>Nick Wilson</b> has directly influenced UK government policy and regulation, leading to the development of tools and guidance to alleviate short and long-term financing problems for large and small businesses and organisations. The research has improved understanding of alternative forms of corporate finance for new ventures, growth and corporate restructuring. Improved knowledge has been gained on why some businesses grow and others fail in relation to financing, financial management and governance. Research has led to changes in the debt management systems and procedures in the public and private sector.</p>
<p><b>2. Underpinning research</b></p> <p>Professor <b>Wilson</b> (at Leeds since 1998), focused on finance and credit management in two main areas: business finance (corporate and small and medium-sized enterprises (SMEs)) and large volume consumer lending and debt collection. Research analysed the availability and quality of credit information, short and long-term business financing; debt collection and recovery systems and methods for improving risk modelling techniques. This work is underpinned by a philosophy that better access to, and use of, information can improve credit management and alleviate financing problems for businesses and organisations. <b>Wilson's</b> research has received support from the Institute of Credit Management (<b>i</b>). The body of research, spanning a 15-year period, was based on quantitative survey methodology, econometric analysis of large databases, and interviews with government departments, utilities and financial services.</p> <p><b>Wilson</b> advised the Department of Trade &amp; Industry (DTI) and authored two influential reports after researching the effects of late payment of commercial debt and SME financing [<b>1</b>]. He was asked to join the Better Payment Practice Group, whose work contributed to the Late Payment of Commercial Debt (Interests) Act 1998).</p> <p>While trade credit affects working capital, a related issue is longer term capital financing. Atanasova and <b>Wilson</b> found that firms' assets can act as collateral in mitigating borrowing constraints. In harsh economic conditions there is disequilibrium in the demand and supply of bank credit, smaller firms increase their reliance on inter-firm credit at certain times and more companies face borrowing constraints during a recession [<b>2</b>]. Altman, Sabato and <b>Wilson</b> found that trade credit is used to compliment/substitute other sources of funds [<b>3</b>].</p> <p><b>Wilson</b> investigated the impact that government legislation on trade credit had on the private sector before 2008; the findings were published by Department for Business Enterprise &amp; Regulatory Reform (BERR)<sup>1</sup> and revealed the vulnerable position of small businesses, the complex causes of late payment and how it causes business failure and distress. Based on a quarterly survey, <b>Wilson</b> produced a late payment index for the private sector from 1997 to 2007 and found that small businesses were reluctant to use legislation enabling them to apply interest rates to late payments; this was reported in the Bank of England Quarterly Bulletins and the report of the Breedon Task Force (2012)<sup>2</sup>. <b>Wilson</b> was invited to join the Expert Economists' sub-group during the preparation of the Breedon report.</p> <p>Regional variations in business financing have also been researched. <b>Wilson</b> analysed variations in the Welsh economy [<b>ii</b>], and his research on business practices among exporters resulted in practitioner guidelines for exporting and credit management professionals being published. His work [<b>4</b>] on the causes of business failure and board diversity was cited in the Davis Report<sup>3</sup> and international press.</p> <p>Working with Mike Wright (Imperial College London), and the British Venture Capital Association (BVCA) [<b>iii</b>], <b>Wilson</b> and Wright published research [<b>5, 6</b>] on the relationship between private equity/venture capital and business growth, profitability and productivity and found that private</p>

equity-backed buyouts are less likely to fail than non private equity-backed buyouts, as well as being more efficient and profitable<sup>4</sup>. This led to work commissioned by NESTA on estimating the equity gap and the results were presented to the Bank of England Financial Stability Division and Policy Advisors' workshop on SME risk and financing in April 2011. **Wilson** worked with Altman and Sabato on improving risk management modelling for bank loans to SMEs [3].

In the field of large-volume lending, CMRC research looked at how large lenders and governments bodies manage customers and collect debt. **Wilson** was commissioned by HMRC and the National Audit Office to benchmark HMRC's debt collection processes against a number of corporate private sector organisations. **Wilson** explored current revenue collection practices, trends and innovations across nine organisations, including major financial services companies, energy companies, a water company and a debt collection agency. The findings were distilled into a best practice model which was compared against HMRC's current debt collection processes. The majority of the recommendations were implemented by HMRC and revealed the need for a reorganisation of HMRC systems and procedures. Similar research carried out for UK Water Industries Research had significant policy issues; **Wilson** joined the Debt Focus Group which reported to DEFRA.

<sup>1</sup>**Wilson, N.**, (2008), *An Investigation into Payment Trends and Behaviour 1997-2007*, Policy Report, Department for Business Enterprise & Regulatory Reform.

<sup>2</sup>Department for Business, Innovation and Skills, (2012), *Boosting finance options for business, Report of industry-led working group on alternative debt markets*, March, URN:[12/668].

<sup>3</sup>Department for Business, Innovation and Skills, (2011), *Women on Boards*, Report by Lord Davies, February

<sup>4</sup>BVCA Reports: **Wilson, N.**, Wright, M. and Scholes, L., (2011), *Private Equity Portfolio Company Performance Through The Recession* and **Wilson, N.**, Wright, M and Cressy, R (2010), *Private Equity and Insolvency*.

### 3. References to the research

- [1] Peel, M.J., **Wilson, N.** and Howorth, C., (2000), 'Late Payment and Credit Management in the Small Firm Sector: Some Empirical Evidence', *International Small Business Journal*, Volume 18, 17-37, doi:10.1177/0266242600182001
- [2] Atanasova, C.V. and **Wilson, N.**, (2004), 'Disequilibrium in the UK Corporate Loan Market', *Journal of Banking & Finance*, Volume 28 (3), 595-614, doi:10.1016/S0378-4266(03)00037-2
- [3] Altman, E., Sabato, G. and **Wilson, N.**, (2010), 'The Value of Non-Financial Information in Small and Medium Sized Enterprise Risk Management', *Journal of Credit Risk*, Volume 6 (2), 95-127,
- [4] **Wilson, N.**, Wright, M. and **Altanlar, A.**, (2013), 'The survival of newly-incorporated companies and founding director characteristics', *International Small Business Journal*, Published online before print February 25, 2013, doi:10.1177/0266242613476317
- [5] **Wilson, N.**, Wright, M., Siegel, D.S. and Scholes, L., (2012), 'Private Equity Portfolio Company Performance During The Global Recession', *Journal of Corporate Finance*, Volume 18 (1), 193-205, doi:10.1016/j.jcorpfin.2011.11.008
- [6] Wright, M. and **Wilson, N.**, (2013), 'Private Equity, Buyouts and Insolvency Risk', *Journal of Business Finance and Accounting*, Volume 40 (7-8), 949-900, doi:10.1111/jbfa.12042

### Research Grants

- (i) **Wilson, N.**, Institute of Credit Management, ICM Chair in Credit Management, (1998-2003): £400,000 and (2003-2008): £235,000
- (ii) **Wilson, N.** with Swansea University – funded by Welsh Assembly, (2011), 'Past, present and future: The comparative performance and sustainability of high growth firms in Wales', £8016
- (iii) **Wilson, N.** with **Clacher, I.**, **Veronesi, G.** and **Altanlar, A.**, Institute of Small Business and Entrepreneurship (Rake Fund), (2011), 'An analysis of UK Regional Development Agency support on company value: evidence from Yorkshire Forward', £11812
- (iv) **Wilson, N.**, British Venture Capital Association, (2009) 'Private Equity and Insolvency Risk', £8000

#### 4. Details of the impact

##### Policy

CMRC's work on trade credit and SME financing has fed into the development of UK national policy and legislation over a number of years. This work has been highly regarded by the UK government and the small business community, which is acknowledged by BIS [A]. The 2008 BERR Policy Report<sup>1</sup> on payment trends and behaviour helped policymakers understand the significance of trade credit and its overall role in business financing as well as the impact of cyclical variations. This report was used by Institute for Chartered Accountants in England & Wales (ICAEW) in their comments to The Insolvency Service on 'Reforms to the regulation of insolvency practitioners' [B]. The Bank of England utilised CMRC data to track SME lending and CMRC research in their examination of SME finance, highlighted issues relating to credit rationing, the credit information infrastructure and competition in corporate lending [C].

The CMRC's work has also contributed to increased knowledge of alternative sources of business finance. The BVCA struggled against negative public perceptions that equity backed lending was linked to short-termism and increased insolvency risk; it was able to use CMRC research to objectively demonstrate that businesses could make better use of alternative forms of business finance. The BVCA published evidence [D] and also influenced government to adopt a more positive attitude to private equity finance [E]. The Chief Economist and Director of Research at BVCA commented "*This study [see <sup>4</sup> above] helped address some of the misconceptions around the PE industry and the role of leverage, and was highly influential when meeting with policymakers, setting fears to rest about the impact of leverage and the need for tighter controls or regulation*" [D].

Findings from the two areas of work on trade credit and alternative business finance were considered by the Breendon Task Force (BIS 2012). The Expert Economists' sub-group were responsible for ensuring that the evidence feeding into the Breendon Taskforce policy discussions was both robust and comprehensive. The Taskforce's final report and recommendations ahead of the 2012 Budget included practical measures to facilitate the development of alternative markets and Breendon reported that UK SMEs were heavily reliant on bank financing and that there was a significant risk in this reliance on a single source of finance [F] – this letter from BIS Economic Adviser acknowledges **Wilson's** contribution to the Taskforce and confirms that the Taskforce report was influential in shaping UK SME finance policy. A further recommendation advocated greater credit data sharing with non-bank providers to support the development of new finance products and markets to benefit business. **Wilson's** research on alternative financing was acknowledged by The Rt. Hon. Dr. Vince Cable, MP, Secretary of State [G] who commented that the research showing that private equity buyouts performed more strongly than buyouts using other types of funding was useful: "*This is quite an interesting conclusion that goes against accepted wisdom but is quite relevant in terms of the work of this department [BIS] in promoting non-bank finance*". The Government accepted the analysis set out in the Breendon Report and agreed that more can, and should, be done to build alternative markets and unlock new pools of capital. **Wilson** has published a guide for SME's seeking sources of funding<sup>5</sup>.

The Expert Working Group on Consumer Credit Information (2008) used research on large volume lenders and problems with payment resulting from individual consumer debt and advised government on how to improve information about individual consumer debt and systems to enable government/organisations make better decisions around lending, collections and recovery [H]. The CMRC's Debt Survey, published by HMSO, helped promote good practice amongst large volume lenders and was a key publication informing the Expert Working Group. The Independent Commission on Banking public forum panel (2010) invited **Wilson** as an expert member of the panel.

##### Practice

CMRC's work has also altered behaviour in the public and private sectors. Research on credit information, risk scoring and best practice in debt management in the private sector was used by HMRC and the NAO in studies of debt management in government. CMRC demonstrated to the HMRC that its systems and procedures for handling tax debt were inefficient, as was the standardised approach used to recovery and the lack of joint working between tax inspectors

(responsible for calculating tax due) and debt collectors (responsible for recovery). **Wilson's** role in advising HMRC is reported in *'HM Revenue & Customs Management of Tax Debt'* (2008) [I] which also details the Government's progress in implementing the changes at that point. CMRC recommended using different strategies for recovery and a restructuring of the processing systems, together with better liaison between departments. Many of the recommendations have been adopted, e.g. the HMRC now use two private companies to improve their information infrastructure and scoring systems.

*'The NAO's work on HM Revenue & Customs: A Short Guide'* (June 2010) reports an improvement in the telephone contact centre's calls answered from 57% to 77% (2008/09 to 2009/10) [I]. The report confirms that HMRC improved the way it manages tax debt and new strategic objective indicators are being used in relation to measuring debt (e.g. debt collected within 30 and 90 days) and the department is tailoring its interventions according to previous risk behaviour, risk and ability to pay [I]. These recommendations were made by CMRC [J].

At workshops with senior figures from major debt collection companies and utilities and HMRC, the use of information and the development of sophisticated scoring and collection/recovery systems were discussed. Research carried out on behalf of the water industry (the Cross Industry Debt Focus Group; UK Water Industry Research and DEFRA) on consumer debt recovery identified problems around recovery and collection companies and identified 'best practice in the sector' and the factors associated with collection success and write-off rates. CMRC proposals were adopted by the industry. CMRC has helped to implement a Voluntary Code of Best Payment Practice for use at large institutions and corporations, which has been promoted by government [K]. CMRC events and forums have enabled government and major service providers such as utilities to share best practice and learn from industry as well as improving awareness of credit management.

CMRC's research contributed to the creation of a University spin-out company, CreditScorer Ltd, which developed on-line benchmarking and risk management services for businesses and utilities. **Wilson's** work in developing algorithms that generate real time risk scores and default probabilities also contributed to the foundation of another business, paymentleague.com, which provides rankings of payment performance by big companies.

<sup>5</sup> <http://www.cmrc.co.uk/conferences/alternative-sources-of-finance-for-smes/>

## 5. Sources to corroborate the impact

- [A] Letter from Assistant Director, Innovation Policy, Department for Business, Innovation & Skills, 21 December 2012
- [B] Response by Institute of Chartered Accountants in England & Wales to the consultation paper *Reforms to the regulation of insolvency practitioners* published by The Insolvency Service, (see page 3, paragraph 13)
- [C] Bank of England Quarterly Bulletin (2013) Quarter 1, Private equity and financial stability, <http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/2013/qb130104.pdf> [downloaded 15/10/13] (see pages 42 and 43)
- [D] Letter from the Chief Economist and Director of Research, British Venture Capital Association
- [E] 'Testing the Model: Private equity faces a more hostile world', *The Economist*, 9<sup>th</sup> July 2009
- [F] Letter from Economic Advisor, Department for Business Innovation & Skills regarding contribution to the Breedon Task Force and Economists' Expert Panel
- [G] Video recording of the Secretary of State for Business Innovation & Skills, at Making the Case for the Social Sciences, at the Society for the Advancement of Management Studies and the Academy of Social Sciences, BIS conference centre in London on 18<sup>th</sup> June 2012
- [H] 'The Science of Business: Britain's under-seige economy shaping up for a double hit' Yorkshire Post, 18th August 2009
- [I] National Audit Office, (2010), *The NAO's work on HM Revenue & Customs, A Short Guide*
- [J] National Audit Office, (2008), *HM Revenue & Customs Management of Tax Debt, Report by the Comptroller and Auditor General/HC 1152 Session 2007-2008, November.* [Page 32 acknowledges the role of Professor **Wilson**]
- [K] 'Debt chasers accused of bullying calls and threats, The Observer, Sunday 28 June 2009