



Key Operational Capability Strengths		Key Risk Factors
<p><b>Analyst</b> Philip Bayley (03) 8080 6684 philip.bayley@australiaratings.com</p> <p><b>Operational Capability Assessment Ranking - Superior</b> A Superior ranking reflects our opinion of the highest capacity to perform, supported by many superior operational abilities. This assessment represents the highest capacity to meet performance expectations in a timely manner.</p>	<ul style="list-style-type: none"> <li>AssetWatch is an automated receivables management system with only minimal manual intervention required.</li> <li>Comprehensive in-built quality controls and risk management features.</li> <li>Comprehensive system support.</li> <li>Facilitates efficient management of trade receivables.</li> <li>Daily calculation, reconciliation and reporting of receivable financing.</li> <li>System is flexible, scalable and fully integrated.</li> </ul>	<ul style="list-style-type: none"> <li>The calculation module that determines the required credit support is not integrated into the platform but operates as a stand-alone module.</li> <li>There is some manual data input which relies on staff to check accuracy and currency of data.</li> </ul>

**OCA Ranking - "SUPERIOR"**

The 'Superior' Operational Capability Assessment assigned to the AssetWatch Trade Receivable Management System ("AssetWatch") primarily reflects the operational and technical quality of the system. The system has been in operation for more than 13 years and in that time has proved its value as a trade receivables management system alone, through the acquisition of servicing only clients in addition to finance clients.

System operation is well documented with all parties aware of their operational responsibilities. Business continuity and disaster recovery plans are in place and annual system audits are a feature.

AssetWatch is a specialist receivables management application derived from an enterprise wide custom software solution developed by Assetinsure. AssetWatch can act as a hot or warm backup servicer for clients, if required.

The controls built into the operation of the AssetWatch system are considered to be Superior to those seen in similar systems elsewhere.

Multiple layers of assessment are a feature of the trade receivables finance origination process, involving sign-off by at least three independent parties.

**Table 1: Ranking of AssetWatch's operational components**

System Ownership, Performance, Outlook	Superior
Governance – AssetWatch Operation	Very Strong
Governance - Trade Receivables Financing Facility Origination	Superior
AssetWatch - System and Technology	Superior
Risk Management and Compliance	Superior
Management and Key Staff	Superior
Financial Adequacy and Stability	Strong

**System Ownership, Performance, Outlook**

AssetWatch is a trade receivables management system owned by Assetsecure Pty Limited (Assetsecure). Executives of Assetsecure are the largest shareholder group with a combined shareholding of 37.38%. 255 Finance Investments Pty Ltd is the next largest shareholder in Assetsecure, with a holding of 33%, followed by various former shareholders of Assetinsure Pty Limited (Assetinsure). (Assetinsure has been purchased by Lombard Insurance Company Limited of South Africa, subject to APRA approval).

Assetinsure is the developer of the AssetWatch system and original owner. Assetinsure is an APRA regulated insurance company and through Assetsecure, originally a wholly-owned subsidiary, has operated as a trade receivables financing and servicing specialist for more than thirteen years.

Changes to the calculation of regulatory capital for insurance companies necessitated the legal separation of Assetsecure from Assetinsure. Assetsecure has operated as an independent entity since the beginning of 2013, under AFSL No. 409144. With the separation, Assetsecure bought the AssetWatch system from Assetinsure, and entered into an extended software services agreement for system maintenance and database access.

The sale of the AssetWatch system is documented under the Software Assignment Deed dated 1 January 2013. The deed allows the purchase price for the AssetWatch system to be paid in five equal annual instalments commencing from 31 December 2013. However, two outstanding instalments were prepaid at the end of fiscal 2016.

Despite the separation of Assetsecure from Assetinsure and subsequent changes in the ownership of Assetinsure, operation of the AssetWatch system appears to be continuing in the same manner as it has historically. The employees and executives of both Assetsecure and Assetinsure continue to work together much as they have done in the past, and the activities of Assetsecure are considered to be complementary to those of Assetinsure.

The assessment of System Ownership, Performance, Outlook is maintained at Superior.

### Governance – AssetWatch Operation

AssetWatch is an extension of an enterprise level custom software solution developed and operated by Assetinsure and licensed to other insurance and reinsurance companies. The Software Services Agreement, also dated 1 January 2013, requires Assetinsure to facilitate AssetWatch system access and to maintain and develop the system as required by Assetsecure. Under the agreement, Assetinsure is required to develop a business continuity plan and ensure that implementation of the plan is viable.

Each party to the Software Services Agreement is entitled to undertake an annual audit of the other party's performance under the agreement. At the time of our 2015 review, two external audits recently carried-out by Grant Thornton and Ernst & Young, identified some shortcomings in the procedures of Assetinsure and the operation of the AssetWatch system respectively. A subsequent audit by KPMG of the procedures carried out by Assetinsure over the

2015 calendar year, revealed no shortcomings and the 2016 audit by Ernst & Young made the same findings in relation to the AssetWatch system. Deloitte Australia has since taken over the audit of the Assetinsure/AssetWatch system and provided a clean audit report in February 2018.

Should Assetinsure fail to perform under the Software Services Agreement there is little recourse available to Assetsecure, other than to terminate the agreement. Termination provisions in the Software Services Agreement require a substantial notice period be given by Assetinsure to Assetsecure.

AssetWatch was developed by the Assetinsure technical team. The IT team comprises 20 staff with combined experience of over 100 years at Assetinsure. This same team supports the current system and continues to maintain responsibility for system fixes, modifications and enhancements.

The technical team are experienced in both IT and the insurance and trade receivables financing industries. This creates a unique and high-quality team that has the ability to interpret business requirements and quickly progress the requirements into system adaptations. All technical staff learn the business, and work across development, support and project management, thereby mitigating key person risk within the technical team. The majority of the technical staff has a strong understanding of the AssetWatch architecture, business purpose and rules. The technical procedures and policies followed by the Assetinsure IT team are subject to continuous review and are audited quarterly in relation to compliance, process and deliverables. User training is provided to Assetsecure employees by the Assetinsure technical team, as needed.

Business continuity and disaster recovery is addressed by maintaining a remote site in North Ryde that replicates AssetWatch data every five to ten minutes. In the event of disaster, Assetsecure employees can work from home and log-in to the remote site. The disaster recovery system is tested annually.

While the documentation governing the software service support to be provided by Assetinsure in relation to the AssetWatch system is considered Adequate, in practice operational support is considered to be Very Strong.

### Governance - Trade Receivables Financing Facility Origination

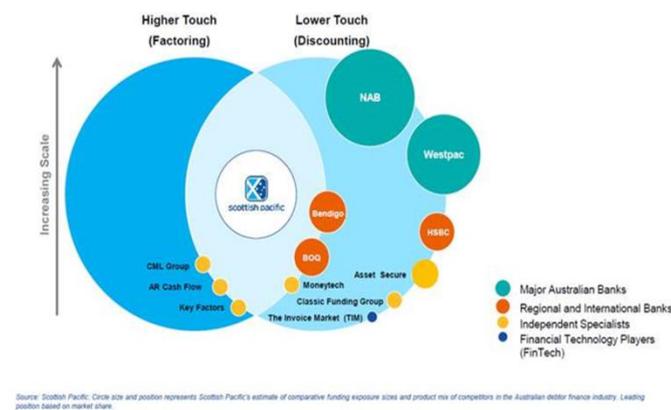
Governance around the origination process for providing trade receivables financing facilities is considered to be Superior due to the multiple layers of assessment in the

origination process. These layers consist of the use of independent accounting firms to carry out due diligence on receivables sellers, to transactional sign-off from the Assetsecure executive, transaction funders and an external insurer, if required.

Assetsecure is a niche arranger of trade receivables financing, whose closest competitor in terms of the size and scale of facilities provided is Scottish Pacific Group Limited (ScotPac), a specialist business finance company. In 2016, Moneytech Limited entered the business finance sector (receivables financing) with a recently secured wholesale funding line from one of the major banks, and joined the ranks of a number of smaller competitors.

Diagram 1 below illustrates the competitive landscape as presented by Scotpac in its 2016 prospectus for its listing on the ASX. Assetsecure argues that its relative scale as presented in the diagram is substantially understated, particularly given the increased business generated over the course of this year.

**Diagram 1**



National Australia Bank and Westpac Banking Corporation continue to be providers of larger receivables purchase or financing facilities via their business and institutional banking businesses, respectively. However, while CBA and ANZ exited this line of business in 2016, both Nab and Westpac are now pulling back as is HSBC, opening up opportunities for Assetsecure to grow.

Assetsecure uses securitisation to fund receivables purchase facilities currently ranging from \$5 million to \$150 million in size, with clients spread across industry sectors such as logistics, wholesaling, litigation funding, equipment hire and manufacturing. Over 2017, a lot of growth was seen in facilities of \$5 million to \$15 million in size.

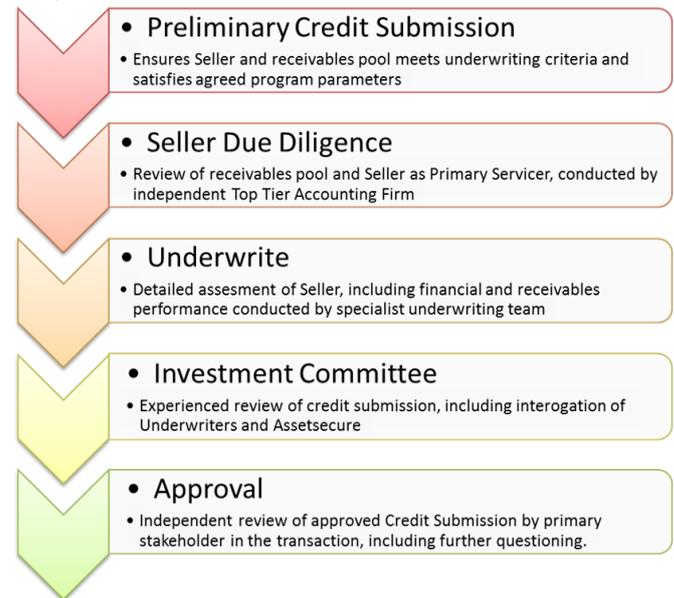
A master trust structure is used to house the receivables purchased, with a sub-trust utilised to hold the receivables purchased under each receivable purchase facility extended

to AssetWatch clients. The operation of the trusts and the issuance of asset backed securities are governed by the Master Trust and Security Trust Deed.

Business origination relies on referrals from business advisors, investment banks and accountants, with whom Assetsecure has established strategic alliances, and two senior managers with responsibility for business origination. Assetsecure’s interest in a potential client will be determined by the size of the receivables pool and the quality of the receivables. The receivables must be unconditional obligations of the debtor and Assetsecure will fund up to 85% of eligible receivables.

On average, establishment of a receivables purchase facility takes around four to six weeks, once Assetsecure is mandated. The process is documented in Assetsecure’s Underwriting Guidelines, Program Operations and Risk Management instructions and Origination and Asset Management procedures. The Program Operations and Risk Management instructions set out the origination process as presented in Diagram 2.

**Diagram 2**



A credit submission is prepared; the funders of the sub-trust that will be used to hold the receivables must be consulted, and independent, top tier accountants are used to carry out the necessary due diligence on the receivables seller, including a historical analysis of the suitability and value of the receivables for use within an asset backed securitisation structure. This assessment includes use of an in-house model based on credit rating agency criteria for securitisation. If credit enhancement is required, a credit enhancement insurance policy will be arranged with an external insurer

before final underwriting sign-off is given by Assetsecure and its funders.

Only sellers with a strong credit profile as outlined below will be considered:

- strong management team
- \$50 million plus revenue, EBITDA \$4 million plus, strong demonstrated cash flow/profitability
- business has a strong market position with established, stable customer base, supply sources and operational proven long track record
- debt service of at least 2 times senior debt
- company should be well capitalised
- good reporting systems
- strong compliance and governance standards
- facility size of \$5 million or more

Assetsecure will take a second ranking General Security Deed over receivable sellers and trade credit insurance is obtained for any debtor that exceeds 2% of the receivables pool, if not assessed as being of investment grade credit risk. Trade credit insurance is typically provided by QBE Insurance Group, Euler Hermes, and Atradius.

Governance of the origination of new financing commitments is ranked as Superior.

- detailed invoice data
- daily reconciliation of transactional data, including cash
- accounting for facility parameters, credit and collection policies, eligibility criteria and other compliance considerations
- single picture reporting for multiple ledgers/geographies
- daily automated upload facilitates ‘real-time’ reporting and mitigates risk of fraud
- customisable reporting

In addition, the AssetWatch system has proved to be a valuable receivables management tool that does not need to be linked to receivables financing. The AssetWatch reporting system has generated tangible working capital savings for clients, including those domiciled overseas. Assetsecure has servicing-only clients and views this as a growth area for the future. Servicing-only arrangements provide the opportunity to extend receivables purchase facilities at a later date.

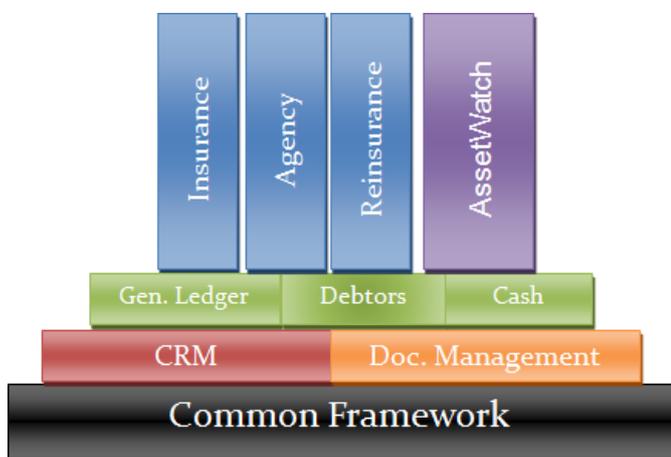
Given the ability of the AssetWatch system to provide ‘real time’ reporting on invoice data; deal with multiple ledgers and locations; and provide daily cash and bank account reconciliation, sufficient to generate working capital savings for third party users, the AssetWatch system and technology is assessed as being Superior to other comparable systems in use.

The AssetWatch User Guide provides detailed instructions on how to use the AssetWatch system. Diagram 4 illustrates the typical process flow, starting with the client, the invoice seller.

**AssetWatch - System and Technology**

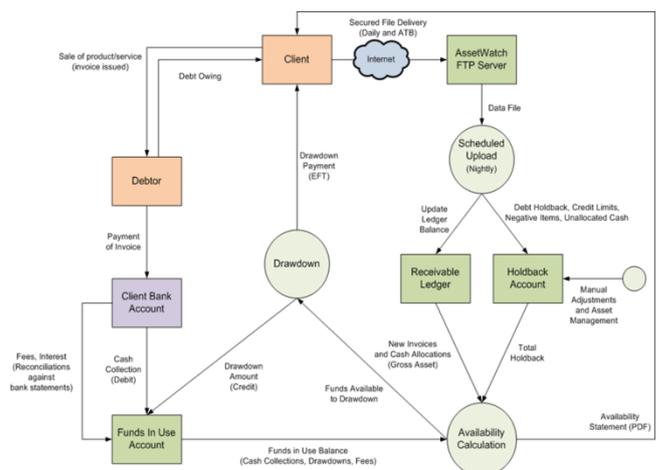
AssetWatch is a module of an enterprise wide custom software solution developed by Assetinsure - first developed in 1988 and licenced for use to various third parties. The insurance, agency, reinsurance and AssetWatch modules share a common basic functionality, as shown in Diagram 3.

**Diagram 3**



AssetWatch reporting provides:

**Diagram 4**

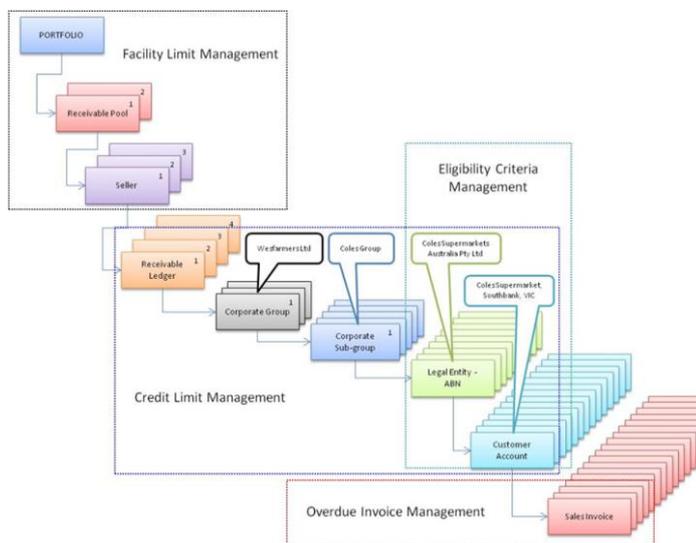


While the AssetWatch system is all but fully automated, some manual intervention is required.

Assetsecure has joined SWIFT, which allows bank statements to be received directly into AssetWatch. AssetWatch then post items automatically into statements and the information generated can be presented in the form of a reconciliation dashboard. The next step will be the generation of payment files, which can be sent directly to banks for actioning.

The information hierarchy employed by AssetWatch allows for the existence of a number of legal entities within a corporate group, be it the seller or the debtor. AssetWatch has the ability to upload any number of data files either from each legal entity within a corporate group, or one data file to cover all legal entities within the corporate group. This information hierarchy ensures that any securitised assets are appropriately separated and flagged accordingly within AssetWatch. Diagram 5 sets out the information hierarchy.

**Diagram 5**



A range of data and rules are stored in AssetWatch, including asset, debtor and seller/client data, eligibility criteria and credit limits, cash collection data, purchase price and drawdown calculations, financing data and general ledger entries. AssetWatch has the ability to set credit limits and other rules at each level of the information hierarchy. A benefit of the platform is that there is no limitation on the number of debtor and seller/client entity hierarchy levels that can be entered.

AssetWatch can act as a hot and warm backup servicer. AssetWatch contains standard correspondence that can be automatically generated within a matter of hours in the event of a seller default or ceasing to service receivables. This has been successfully implemented in the past. However, in the normal course of operations the seller remains the primary

servicer of the receivable and the existence of Assetsecure/AssetWatch should be invisible to the debtor.

Certain information is stored in AssetWatch via manual entry, including:

- the full hold-back flag (i.e. an indicator as to whether the receivables are purchased at no cost due to the breach of certain eligibility criteria such as an unknown ABN)
- the monthly debt hold-back percentage (determined initially as part of the pre-settlement due diligence and then verified monthly by a separate advance rate model)
- hold-back adjustments for certain items, such as unallocated cash
- the facility limit and the seller entity credit limit
- the base rate used in the calculation of the usage fee

It should be noted that Assetsecure has rigorous input and approval processes to minimise the risk of input errors. In addition, a number of rules associated with calculation and reconciliation elsewhere in the platform facilitate detection of data entry errors.

Before a new client/seller is allowed to access AssetWatch, a two to three week trial of receivables uploading over the seller’s month end is undertaken. Any problems encountered by the platform including data corruption will be flagged at this time. Drawdowns from the sale of receivables are only possible after the trial period has been successfully completed. Under the trial process:

- The entity is provided with a “Data Upload Format Specification” document. This document specifies the format (XML) and schema by which daily data must be supplied.
- Assetinsure’s technical team work with the entity’s technical and business teams to ensure that the entity’s data fields are correctly mapped to the required specification.
- Testing occurs until the mapping is deemed to be correct. This testing encompasses reconciliations and checks against manually performed calculations.
- Data is transmitted from the client/seller to AssetWatch via secure FTP.

AssetWatch is an extension of an enterprise level custom software solution that was developed by Assetinsure to cater for the corporate insurance and reinsurance industries. AssetWatch is built using Microsoft technologies, including

Microsoft SQL server, and is written using C# programming language.

Use cases act as technical system documentation, which outline user workflow, business rules for each function, and technical considerations. A technical data dictionary also exists.

The data is captured via an XML schema, which enables flexibility to capture just the mandatory data, or as much additional data as may be available from the seller/client entity.

The System has substantial capacity, with the backend running on servers that can be scaled, as required. All system support and requests for fixes, modifications and enhancements are provided by Assetinsure's technical team, via a helpdesk arrangement. Each request is logged in detail. An informal review of all logged requests occurs every few days, and a formal review occurs monthly as part of the change control committee. This assists in identifying any concerning trends or weaknesses in the platform or its use and output.

Logins and user account protocols ensure adequate System security.

The controls built into the operation of the AssetWatch system are considered to be Superior to those seen in similar systems elsewhere, with only a very low level of manual intervention being required.

The systems and technology that underpin AssetWatch are ranked as Superior.

## Risk Management and Compliance

AssetWatch contains a range of comprehensive controls, error detectors and risk management measures including:

- Sellers cannot interface directly with the system, but instead receive daily standardised reports via automated email. Seller data is transferred daily via FTP and uploaded to the system by Assetsecure. This greatly reduces the risk of fraud and human error.
- Each client is established in AssetWatch in a dedicated database, separated from all other client databases. This ensures there is no cross-contamination of data and minimises the consequences of human error.
- User rights can be set up to restrict access to any online function. This assists with segregation of duties. In addition, authorisations and delegations are built into the system user rights to enable

automated authorisation workflow via an email sent to the authoriser.

- A login-specific audit trail exists for every insertion, deletion and modification within the System. Sample audit and activity reports can be run to reflect this.
- The daily process consists of a number of key milestones, and AssetWatch operates such that certain milestones must occur before the next milestone can begin. For example, a drawdown cannot be processed unless the previous milestones have been completed. This means that funding cannot occur until data has been uploaded and all reconciliations have occurred.
- A range of user and technical procedures and policies are available in soft and hard copy. These documents are reviewed annually to ensure currency.
- A formalised change request protocol exists, with change requests being efficiently and promptly responded to as part of a managed risk process.
- Seller data cannot be edited once uploaded into the system.
- AssetWatch provides for a sampling of invoices, by automatically sending an email directly to the obligor requesting invoice confirmation. The audit sample rules are maintained within the system, and can be varied to tailor for individual seller entities. If debtors do not respond to the email, Assetsecure will endeavour to verify the invoice using other means, such as telephoning the debtor.
- AssetWatch has a screen which flags any data or calculated information which signals significant changes in invoice volumes or changes to the aging profile. This is also available in a report format, and once again, the rules can be tailored as required.

A number of the controls listed above have enabled Assetsecure to detect possible fraudulent activities, including mis-bankings, and re-ageing of receivables. The system has also been tested by the failure of a seller, which was dealt with by the collection of outstanding invoices in the normal course of business, and the wind-down of the seller's receivables finance facility as collections were made.

Risk management and compliance is assessed as being Superior.

## Management and Key Staff

Assetsecure currently comprises a lean team of ten people including:

Terry Hartan, Chief Executive Officer – is a chartered accountant. Terry is responsible for the overall operations of Assetsecure, including origination of new business and sourcing third party financiers/investors.

Duncan Alexander, Chief Operating Officer – is a chartered accountant and is responsible for credit risk management, operations, service delivery, accounting, compliance and company secretarial. Duncan is directly involved in the operation of the Assetsecure Floating Rate Note (receivables securitisation) Program.

Geoff Baker, Senior Manager – is a chartered accountant and is responsible for client relationship management, day-to-day operations, credit risk and facility compliance.

Omar Tabbaa, Senior Manager - is responsible for originating and client relationship management, day-to-day operations, credit risk and facility compliance for smaller receivables financing lines of \$5 million to \$15 million. Omar has over 12 years' experience in financial and telco services, and risk management.

Tim Barrett, Senior Manager - has over 20 years broad business and financial service and structured trade finance experience, in Australian and global jurisdictions. He took responsibility for originating receivables financing facilities in Queensland in mid-2017.

Elyssa Crozier, Head of Operational Risk - has over 7 years' experience in financial services, managing operational risk and compliance. Elyssa works with Duncan Alexander focusing on internal audit and compliance.

The team is expected to expand as new business opportunities are realised.

The two senior executives of Assetsecure have many years of experience in trade receivables financing and as shareholders in Assetsecure, have a sizeable investment in the success of the company. Key man risk within the team has been addressed with Geoff Baker, Omar Tabbaa, Tim Barret and Elyssa Crozier all bringing more senior and complementary experience to the firm. KPMG has also been appointed as a back-up servicer to Assetsecure.

The assessment of this aspect of the operation of the AssetWatch system is Superior.

establishment and arranging fees, asset management fees, and residual income from the sub-trusts that hold the receivables.

Assetsecure is highly profitable, has professional indemnity insurance cover up to \$10 million, and in need, might expect support from its major shareholders.

Financial adequacy and stability is assessed as being Strong.

### Financial Adequacy and Stability

As an originator and manager, rather than a funder of trade receivables, Assetsecure can maintain a modest balance sheet in comparison to its much larger competitors in the trade receivables financing market. Income is generated from

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