remedy
taking care of business

Credit management checklist

Today, few companies can hope to survive unless they offer some form of trade credit. A company that decides to extend credit to its customers accepts a risk. The company is, in effect, lending its money to its customers. There is always a risk in lending money, and there are two areas of risk: the risk of bad debt and the risk that customers will not pay by the due date.

The bad debt is a total loss. The company has provided its goods or services and is not going to be paid. Because of the risk, companies make a provision for this and in accepting the risk, they also accept that some bad debt is likely to arise.

The second area of risk, the slow payer, is not often perceived as such a problem. After all, we will get paid, eventually. It is not a case of bad debt, we just have to wait for our money. This philosophy ignores the fact that slow payers erode your profit. Most companies are subject to the 80/20 rule, i.e. 80% of business comes from 20% of their customers. Very often that 20% will contain an element of slow payers.

Of course, when these customers do pay, they pay substantial sums. That can deceive us into a sense of false security. We get a lot of cash in a particular month but, in fact, the customer is making payments “on account” and is constantly exceeding your terms.

Credit Policy

All organisations need rules and regulations. Every company should have, or use, some form of Terms and Conditions of Sale as the rules and regulations which govern trading with a customer. But how many companies have a written down credit policy? A Credit Policy is an important document as it provides internal controls to ensure that selling and collecting on credit are handled efficiently, and in the best interest of the company. Because of this, many companies see it as a financial tool.

Although it is a document for protecting the financial health of the company it should also ensure high levels of customer service. It is, therefore, more than just a financial document. It is a set of rules which have to be accepted by both finance and sales departments if it is to be workable. It has to be one that ensures financial issues are supported whilst supporting Sales in their efforts to sell.

Factors influencing your Credit Policy

1.) Terms of Business

Do they specify when you want to be paid?
Are they clearly printed in plain English and concise?
What documentation is used to advise the customer of your terms?
· A separate document.
· Confirmation of order.
· Credit application form.

· Invoice.
· Statement.
· Collection letter.
Is there any inconsistency between the terms printed on one document and another?

2.) Credit responsibilities and authorities

Who has the authority to give credit?
· Salesforce.
· Credit department.
· Sales manager
· Other.
Is that authority limited in any way?
Is any credit assessment carried out? If so, by:
· Credit Department.
· Salesforce.
· Sales Manager.
· Other.
Who has responsibility for:
· Account collection?
· Stopping supply.
· Authorising the use of a collection agency or legal action.

3.) Knowledge and expertise

Are salesforce aware of your terms of business?
Do they sell them to customers?
Have salesforce had sales and credit training?
Have your credit staff had any specialist training in credit assessment, account collection and legal procedures?
Do sales meetings include a review of overdue accounts?

4.) Your market

Do you know what credit terms your competitors offer?
Are they the same as yours?
Is your product or service, in comparison to your competitors: as good, better, worse, cheaper, or more expensive?
Do you compete by offering longer credit than your competitors?
Do you need to?

5.) Cost

Do customers regularly exceed your credit terms?
Do you know what giving credit actually costs your company in a year?
Have you, in the past 12 months, incurred a substantial bad debt?

Do you know what cost you incur in:
· Administering accounts?
· Sending statements?
· Sending collection letters?
· Telephone collection?
· Collection agents' commission?
· Legal fees?

6.) Your method of operation

Do you, in practice, give instant credit?
Do you limit the instant credit you give?
Is there a time gap between obtaining the order and the despatch of goods or supply of services?
Do you operate through branches?
Do they have authority to give credit?
Do you have a central credit control function?

7.) Company objectives

What are your terms of trade?
What was your Days Sales Outstanding (DSO) figure last month?
Is that an acceptable level of DSO?
Of the bad debt you incurred last year was some part of it avoidable through better credit control?
Do you currently take a firm line on credit control, and are you considered by your customers as a priority payment?
Are your monthly credit management reports prepared and issued within 48 hours of month end closure, showing:

· Days Sales Outstanding (DSO)
· Cash Collected Against Target
· Level of Overdue Debt
· Query Statistics
· Brought Forward, Raised, Resolved, Carried Forward
· Ageing Analysis from Invoice date and Query identified date
· Value and Number of accounts with Collection Agency
· Value and Number of accounts with Solicitors
· Value of Debt transferred to Bad Debt Ledger
· Value of receipts posted to Bad Debt Ledger
· Total Value in Bad Debt Ledger
· Value of Bad Debt Write off
· Value of Bad Debt Provision
· Value of Credit Note Provision
· Following month’s cash and DSO target

Failure to operate a Policy could mean several kinds of unauthorised actions leading to misunderstandings between Sales and Credit Control. Misunderstandings can be damaging to internal relationships and could also affect a company's policy towards customer service. In order that a Policy is accepted and used, it must be drawn up by both Sales and Finance; form part of any procedural document in Sales and Finance; and should be issued to all staff through a formal presentation that enforces the company's requirement that employees at all levels abide by it.
A credit policy, once formulated, should be reviewed regularly. Outside influences such as a changing market or an economic decline may require changes in the overall corporate credit plan.

Reducing slow payers

A ten point plan helps businesses reduce the number of slow payers and cut bad debts.

1. Know Your Customer
Is your customer a sole trader, partnership or limited company? Make it your business to know their creditworthiness. When a debtor pays on time, its precise legal identity seems irrelevant. As soon as payment stops, this identity becomes very relevant. Often the only clue is the name on an Invoice, usually a trading name that gives no hint of the legal entity behind the business. This is where credit reports prove invaluable.

2. Setting Credit Limits
Set conservative credit limits for new customers and don't be afraid of dealing on a payment in advance basis with some companies. For example, if you want to do business with a new company but are unhappy about giving credit, a personal guarantee from the company's directors to back up the commitment to pay offers a measure of comfort. The guarantee can be just a short letter and need not strike fear into the hearts of new customers.

In addition, a customer should always be asked to sign for goods delivered and you should keep the delivery note. Without it, a straightforward collection of money owed can be spun out by a debtor whose representatives are prepared to testify that the company did not receive the goods.

3. Invoice Promptly
Issue invoices promptly on completion of the order.

4. Reminders
Issue monthly statements and telephone overdue debtors.

5. Obtain Names
When chasing overdue accounts, always obtain the name of the person in the Purchase Ledger department who has authority to promise payment.

6. Be Prepared
Make sure you have all the facts before telephoning a debtor, including checking how many copies of invoices have been sent.

7. Making the Call
Speak clearly and give your name, company and amount involved. Control the conversation and get a firm commitment to payment.

8. Keep Records
Keep accurate notes of all telephone conversations and if necessary, confirm points by e-mail. It is important to make written notes of each telephone call and to follow up the more important calls in writing. This exerts pressure and ensures the debtor cannot wriggle off the hook when you instruct solicitors.

9. Be Prepared to Compromise
If there is an obvious cash flow problem, be prepared to negotiate interim payments on account. Care must be taken in drawing up such plans to ensure that you can still respond quickly to a debtors changing circumstances. It is frustrating to be bound by an instalment agreement only to see "later" creditors leapfrog you in the payment queue.

10. Take Legal Action
If persuasion fails, be prepared to sue the debtor. If your case is successful, you should be able to recover your costs and obtain interest on the original debt. At the end of the day, there is nothing to be gained from allowing overdue accounts to slide and the points mentioned above will help businesses recover payments due to them. Many companies become so preoccupied with day-to-day survival techniques that they often overlook areas from where they can seek advice, or indeed help themselves improve their cash flow.

Excuses, Excuses
In recent years, the debtor has been responsible for many great works of fiction. We are, of course, referring to the increase in the number of excuses for non-payment designed to waylay the busy Credit Control Department.

Companies with a less than tight Credit Control Policy are being exploited, as companies try holding on to their cash for as long as possible. Many businesses get into the habit of paying bills late without thinking about the consequences to their suppliers. The result is that the organisation on the receiving end loses out in the long run, as late payment practices threatens its cash flow, leading to the real possibility of its bankruptcy.

Unfortunately, as the list of excuses for non-payment increases, companies have become far too understanding and ready to accept excuses, however ridiculous they seem. The only solution for those companies awaiting overdue payment of bills is to clarify whether disputed accounts are fact or fiction, whether they are technical or administrative and how they can be amicably sorted out.

Typical Excuses and Responses

"We only pay on statement and you have not sent us one"
Send a copy statement by e-mail immediately.

"Invoices not received"
E-mail duplicates and diary forward for seven days to chase for payment. Although requesting copies of invoices is a well known delaying tactic, the other reasons for this request is that the original invoice was not agreed and simply 'thrown away', or the invoice has gone astray for no other reason than the supplier does not follow the buyer's instructions.

"Invoices disputed"
Do not let this one become an excuse for allowing your invoices and statements to pile-up in someone's in-tray. Request details of when the dispute was first notified to your office, and to whom your customer spoke. If possible try to deal with this dispute over the telephone. It is likely to be a nuisance to them and, if it just an excuse, it is unlikely to resurface again, so the time taken on your part may be well spent. In the event that this is not an excuse but a real reason, then it also means it will be dealt with promptly in accordance with your customer service policy.

"The goods were not up to the required standard"
That is, the goods are allegedly failing to perform to a standard. Under these circumstances you have little choice but to refer this to the appropriate department. And if the goods are at some far flung site, or are part of a larger contract with other manufacturers equipment involved the credit controller need not expect a swift reply. Even so, persistence pays off and it is likely that some aspects of the problem are already known to the credit controller's engineers.

However, we should beware of the engineer who too quickly assures us that we, the supplier, are blameless. It is rarely that simply. We should gather the evidence and speak to the customer and make up our own minds. If we have done our homework it truly is wonderful how often the debtor's arguments fail to materialise into a defence to a well constructed claim which occasionally may have to be accompanied by a High Court writ.

"Awaiting credit notes"
Request details of why credit is due, to whom the customer spoke to regarding the credit and the value of the credit claimed. Ask for immediate payment of any balance outstanding.

"We are currently awaiting funds from a large customer and can only pay you when these funds are received"
It is useful to obtain the name and address of your customer's debtor, the amount that is owed and the expected date for payment. Point out to the customer that Banks are often willing to provide additional funds on security of the debt that is owed to its customer. In the circumstances, you must therefore insist upon receiving your remittance by return.

"We have no money. Any further pressure upon us is likely to force us into liquidation"
If the customer is unable, or unwilling to provide you with a post-dated cheque, then you must rely upon the terms of the retention of title clause in your Conditions of Sale which require the customer to deliver to you your company's goods still in possession of your customer, but which as yet are not paid for.

"We are rearranging our offices and there is some hold-up with the paperwork"
Fine, this can happen once, do not let it become a regular excuse and in this case regular means twice. If you are going to be lied to, at least let it be by a professional.

"Our company is currently changing banks and we have no access to funds"
Explain to the customer that you are willing to accept a manually prepared cheque or a bank draft from their new bank.

"All our accounts are paid at each month end"
As many companies become heavily dependent on computers, this excuse has the best chance of actually being true. After dealing with this customer for a month or so, you will be aware of their end of month cheque run policy. If you are chasing them for overdue payment, it may well be because you did not receive a payment at the end of last month, therefore rendering this excuse invalid. It is important to remember that all companies are susceptible to pressure and can always break out of established payment routines to issue manual cheques.

"Our cheque signatories are all out of the office for a few days"
Find out the names of the individuals within the organisation who are authorised to sign cheques in the absence of the normal cheque signatories, and the earliest date upon which those people will be back in the office. Since the situation may occur in the future, invite the customer to sign and return to you a direct debit form. Diary forward to the date and time when the director is due to return and telephone again.

"Our accounts are with our accountants/auditors"
This is a very common one, and an outrageous lie. In the case of large companies, the source documents almost never leave the client's premises, the auditor goes to them. In the case of smaller companies, the auditor will always make sure that if he has to take currently active documentation away from the premises in order to perform the audit, he will in fact certify copies himself and take the copies, leaving the original documents with the client. In any event, most companies do not send their accounts off to the auditors until several months after the year-end have passed, by which time these matters out to have already been sorted out.

"We are in the middle of a VAT inspection"
Although VAT control visits take place on the client's premises and do not prevent the client from getting to his papers, there are times when the VAT man enters the office in the early hours to take away all the papers. This is only done in very extreme circumstances and if it has happened to your customer, it suggests more than a mere hiccup. Probably your best course of action is to start considering how to account for bad debts in your books. There will be no need to contact the company next month because the VAT man will have sold it to recover his debts, and he's preferential creditor, you're not.

And, of course we have all heard the palpable excuse ***"the cheque's in the post"***. However, in contrast to the above, one of the most outrageous excuses ever received by a company was from a bailiff's report saying the debtor's house had not been entered as a wild tiger was loose in the grounds!

Remember !!

The only way to handle excuses is to treat them for what they are, and get on with the business of collecting your money. If you are not tough enough with debtors, they will go bust, and take you with them !!