Introduction to Credit Management

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Forward

This course starts at the very beginning and assumes the reader is looking at the area of Credit Management for the very first time – I apologise if you think parts of it are too simple – I do ask you to follow the programme because it works – and the purpose is to eliminate all complexity, all grey areas, all events that can add confusion so you have a clear black & white structure to manage your credit function in an efficient, customer friendly, profit focused way.

Make sure you know when you should and when you shouldn't extend credit.

This module will show you how to get a full picture view of your business, how each component should link together for the overall desired effect.

As it is the text for the Certificate in Credit Management it combines an academic understanding with a practical approach to benefit you and your business.

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"Credit has the power to drive your business beyond your ambition. Effectively harness this power and it will prove the foundation of your business success. Let this power of control and it could destroy all your efforts to build a flourishing enterprise"

- Ron Wells

"For your business to be successful you must believe at the outset that getting paid is important to you, and then you must act accordingly"

- Declan Flood

Introduction

Credit is the greatest tool known to man. It enables business that would otherwise be lost. It allows purchasers the opportunity to match the payment duration with the expected life of the purchase – how many new cars would be sold if there was no such thing as credit? How many business start ups would there be if businesspeople had to pay up front for every purchase?

By paying for a large item in instalments it effectively transforms the purchase from a large capital expenditure to a weekly or monthly expense. Most people don't see the €20,000 price of a car they focus instead on the €350 a month it will cost them – and decisions are made on that basis.

Every Credit Controller must take their Credit Function very seriously - way more seriously than ever before. This course gives you a step by step approach to deal with this most important function.

For this course to work, you must be clear that the collection of your money is a very important part of your business and you have to constantly convince senior management of this seemingly obvious fact. You must be committed to delivering excellence and making sure you are adding value to your Company and as a result of what you learn, and more importantly how you apply what you learn every single day.

You should see your role in Credit as a cross between Sales, Finance, Administration, Dispute resolution and sometimes even an agony aunt! You must make sure your customers (not debtors) are happy and you are delivering what you promised – you should also ensure your sales are profitable sales – and if you are seen to really care about these two important areas your value to your employer will increase immeasurably- this course will show you how.

For years companies have been saying things like "A sale is not a sale until it is paid for" and "Cash is king" and other glib remarks and then went and acted in a totally different way. They measured their success through sales and growth; they rewarded sales people for bringing orders into the business. The entire business revolved around the sales process and the collection of the money due was at best an afterthought, and in extreme cases a mere accident of selling.

While saying that "Cash is King" the reality during the good times, that business people could not get rid of cash quickly enough and some used every penny they had and every penny they could get hold of to buy property, shares or whatever they could to give them maximum returns. The reality is that with high returns comes high risk and this fact was ignored or not even considered by some of our most influential business people.

We are now entering a new era for business. In this new era the priorities will change, in this new era, cash will become the focus of all successful businesses; in this new era value for money will be the order of the day. This is a new era, where everybody must add value to their companies in order to secure their own position.

This course is intended as a commonsense manual to help you manage your credit in an intelligent, prudent and commercial way.

The jargon has been removed as far as possible although because it is a course you will learn the correct descriptions and definitions as is relevant. We explain complex concepts in simple language, using simple examples and provide you with the links and information you will need to perform this important function at a level of excellence.

Sometimes when people hear the phrase Credit Management or Credit Control, immediately they assume it is all about the collection of the money. Although the collection process **is** an important part of the function it is not the entire function, in fact, there are a number of things you have to do well to make the job of collecting your money easier.

This function is based on a simple Six step approach summarised in the six letter acronym ATTACK© developed by Declan Flood - The Credit Coach, Internationally recognised expert on Credit management. This six step approach which is central to the course that will give you an in depth understanding of the function and explains what to do and how to do it.

The Six letters stand for:

Assessment

Terms and Conditions

Teamwork

Administration,

Collections

Key performance indicators

The combination of these six steps is the key to overall understanding and management of credit.

In putting the six steps together we believe the steps are in logical order. We also believe that because of the current business environment you have two main concerns: the first one is to collect the money you are now owed, and secondly to set up a procedure for going forward to

The course will also help you implement the necessary controls to protect your business.

To help you inject a sense of urgency into proceedings. Let me share with you, a graph to show the effect the passage of time has on your collection effort as published in "The Credit Management Handbook" edited by Burt Edwards. If your outstanding balance is within terms, you can expect to get 100% of it. If your balance is 60 days beyond terms, you can expect to get 80% of it. If your balance is 180 days beyond terms, you can expect to get 50% of it. If your balance is over 360 days, beyond terms, you can expect to get only 10% of it.

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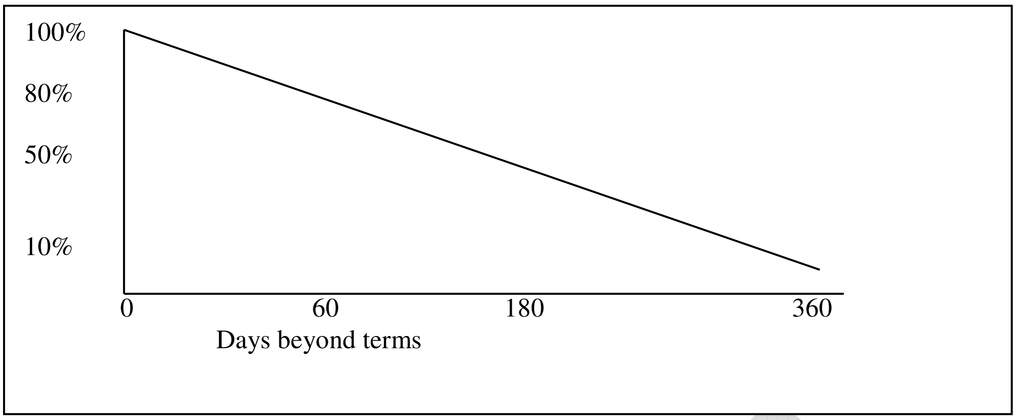
Effect of time on collections



The longer you wait, the less chance you have to collect your money. The longer you leave, a query unresolved, the bigger the credit note you will have to give. As the balance get older, you risk losing the money and the customer altogether.

Part of the new thinking is to develop a profit mindset which will be explained throughout the text.

The first question, you must always ask is “does it make sense?” and in assessing the answer to this question. You must be sure it makes sense for the whole business. To be truly successful the credit function should be viewed as the managers of the margin. Your credit function is well placed to see all aspects of your business, and if properly trained and educated, the person responsible will be able to see where the opportunities are and they will also see where you are letting your customers down, if you let them. Make sure you're capitalising on this important function.

Just so you are clear, this Guideline is produced for information purposes only, we will not accept any liability for errors, omissions or inaccuracy in this document. We see this as an organic document that will continue to grow and expand as new thinking emerges.

Good luck with the implementation of the knowledge contained in this course, your success is our main concern, and I know that your entire business will benefit as a result.

Best wishes,

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Overview of the six elements of our alternative ATTACK® model:

Step 1

Assessment - Setting up new accounts

- Introduction
- Overall approach
- Who are you trusting?
- How much can you trust them with
    - Setting correct lines of credit
- Application Forms
    - Consumer
    - Business 2 Business
- The information you should look for
- Trade References
- Available information
- Credit Assessment
- Customer visits
- Ongoing assessment of existing customers

Step 2

Terms & Conditions

- What are your terms?
- What you should consider depending on your business
- Purpose Contents
- Sample Terms & Conditions
- What it means

Step 3

Teamwork - Working Together

- Sales
- Operations
- Service Departments
- Professional Services
- Building Trade
- Building Relationships
- Working with customers
- Working with & reporting to the board of directors

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Step 4

Administration & Controls

- Credit Policy
- Right first time
- Invoices
- Statements
- Credit Notes
- Cash accounts
- Charging Interest
- Cash Allocation
- Bank Reconciliation

Step 5

Collecting what you are owed

- Where to start
- The correct approach
- Asking to be paid
- Reminders
- Phone calls
- Collection Letters

Step 6

Key Performance Indicators – Reporting

- What you should report on
- Defining responsibility
- Weekly & monthly reviews
- Sample Reports
- Targets
- Action Plans

Hope you will find that our alternative form of ATTACK© makes more sense in your business, as you shift your focus from individual functions to overall profit.

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The course comprises of four modules and for the purpose of maximising your benefit from the course in the quickest possible time the four modules are not in the same order as outlined above.

Module 1 – focuses on Credit Risk Assessment and takes you through all the steps required to deliver excellence in this area, and covers trade, consumer and export credit. This module covers the non-financial issues to be considered, we go into greater detail on scoring models and financial analysis in the Risk Module.

Module 2 – Combines Administration, right first time and KPI's

Module 3 – focuses on Credit Terms, Terms & Conditions, Incoterms and Teamwork

Module 4 – focuses on Collections, from a credit management perspective. As this is the area that most of you work in on a day to day basis, this module should help you approach the job in the best way possible and you will see measurable better results as a result of implementing the techniques as outlined in this module. It will give you an overview of the collection process that we go into in much greater detail within the Collections Module.

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Module 1

Credit Risk Assessment – the non-financial factors

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Introduction

Perhaps the best place to start is with a definition of the word Credit. The word Credit comes from he Latin verb “credere”, which means to believe or to trust. When we give credit we are providing goods and services today, and we trust that our customer will pay us at some time in the future. When we trust anybody with our money there are four fundamental questions we have to ask:

1. Who am I trusting?
2. How much can I trust them with?
3. How long can I trust them for?
4. Are they willing and able to pay the full amount on the due date?

As simple as these questions appear, in my experience they are overlooked by most businesses. In times of economic boom you could probably get away with it, in more difficult economic times you certainly will not, and in the current environment when it looks like we are coming out of the recession is the most dangerous of all. Companies are hungry for business and at times will take on new business at all costs, this often leads to overtrading which has the result of increasing the number of business failures just as things start to pick up, so let's go through each one in detail and make sure you fully understand the significance and the implications of each of these elements, and how you can put the steps in place in your business.

Who am I trusting?

Is the most fundamental question and one that is not asked by most businesses. A customer must be either a person or a partnership or company or a corporation or club or a co-op or an association or a government department. To make sure you're on the right track from the start, it is essential that you bill the correct entity. Step one for existing customers is to check through your debtor’s ledger and make sure all the names are recorded in terms of legal names. There are two types of names – Legal names and Trading names.

Legal names are:

1. Individuals/ Sole Trader, where the person owes the money themselves. This also applies to a sole trader carrying out business in his or her own name – this is perfectly ok and the individuals involved are personally liable for all debts incurred. Bills should be addressed to the individual in person and make sure you have the correct spelling and order for their name. In this category the person owns and controls the business themselves.

Advantages of setting up as a Sole Trader

- A sole trader format is simple to set up.
- There is no formal registration of your business needed before you can start trading.
- It is possible to alter the business format at a later stage.
- You do not need to register the financial accounts for your business.
- As a sole trader you absorb all the profits and all the debt and risks of the business.
- When you retire or die the business comes to an end.
- Sole traders do not pay corporation tax, but will need to file a Return of Income with the Revenue Commissioner every year, under the self-assessment system.

Disadvantages of setting up as a Sole Trader

- Liability is unlimited, so you are responsible for all the money your business owes.
- Possibly greater difficulty in raising finance, as you cannot sell shares and you will not have any partners to invest money.
- A sole trader may often rely on the skill, expertise and experience of just one person; as the business grows, greater demands may be put on their ability.
- Can result in long hours and high stress.
- From a tax perspective a sole trader pays tax at income tax levels on all profits made by the business irrespective of how much or little is drawn out. Companies pay corporation tax which is traditionally at a much lower level.

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2. Trading Style, Individuals can register a business name – if this is done they remain personally liable for all debts incurred. To be absolutely sure in this case you should send out your invoices to Mr John Murphy t/a (trading as) Murphy's Corner Shop. You can check out business names at www.cro.ie

3. **Limited Company** where the company owes the money – these names usually include words like Limited or Ltd. Signifying it is a limited company, Teo. Which is the Irish for Ltd and an acceptable form in Ireland.

International examples of limited companies are:
GmbH - Gesellschaft mit beschränkter Haftung (Limited Liability Company) in Germany, Austria and Switzerland and some Eastern European Countries.

AG – **Aktiengesellschaft –** same countries as above – literally company with shares.

LLC – Limited Liability Company in America

AB – Aktiebolag – Limited Liability in Sweden

ANS - Ansvarlig selskap in Norway – equivalent to our unlimited company

S.A. - *Société Anonyme – usually refers to an international corporation*

For a full list of entities in each country see:
http://en.wikipedia.org/wiki/Types_of_business_entity (for information only, not part of the syllabus)

Plc – signifying the Company is a Public Limited Company – their shares are traded on the stock exchange. It is possible for a company to apply for permission not to use the word Ltd on their letterheads etc.

If a company fails, provided the business has been carried out properly (i.e. not recklessly or fraudulently trading). The directors are not personally liable for the debts of the company. The Company is a separate person in the eyes of the law (more about that in your law module!). Companies must be registered with the Company Registration Office (CRO) and comply with all aspects of the Company's Acts which includes filing certain information on an ongoing basis A Company is a separate legal entity owned by shareholders. It is totally separate from the people who own and run the business. It is an individual in its own right and can enter contracts. In some instances, directors can be requested to give personal guarantees for loans to limited companies.

Advantages

- Ownership is transferable by share ownership.
- Incorporation increases the capacity to raise finance.
- The only income taxable on the owners of the business is any salaries or dividends taken from the business.
- There is often a tax advantage; for example only a limited company can qualify for the lower company tax rate.
- In bad years, losses can be carried forward, and then offset against profits in good years.
- The company theoretically lives forever

Disadvantages

- Setting up involves a number of legal and fiscal formalities, which can be costly.
- Financial accounts and other information must be lodged each year with the Companies Office to comply with the Companies Act.
- Business losses may not be set against personal income.
- There is the possibility of further taxation on capital gains, if appreciating assets are withdrawn from the business.
- There may be a requirement for an annual audit, although this depends on the turnover, balance sheet totals and the number of employees working for the business.
- Lots of form filling and compliance issues to be aware of from the CRO and the Director of Corporate Enforcement.

One other thing you must be aware of with Limited Companies – Companies can act as parents to subsidiary companies – you really have to look at the structure and know exactly who you are dealing with. You could be doing business with ABC Ltd – a major world Corporation and a blue chip Company. Check the small print because you may be dealing with ABC (Ireland) Ltd, A wholly owned subsidiary – and a complete separate entity from the parent, that may or may not have sufficient financial strength in its own right.

4. Partnerships, where two or more people come together to do business without setting up a limited company. In this case each of the partners are liable for all the debts of the company. A partnership is where 2 to 20 people form a business together. Often Accountants or Solicitors practices are operated in this format. All partners can be involved in running the business, but sometimes there can be a "sleeping" partner where he/she has invested money in the business, but is not involved in running it. If you plan to trade using anything other than the partner's names, you will need to register your trading name with the Registrar of Business Names. Partnerships (including limited partnerships) are also obliged to prepare accounts and submit them to the Companies Registration Office.

Advantages

- Easy to set up and subject to minimal regulations.
- All the partners share the profits and all the debt and risks of the business in a pre arranged percentage.
- The partners experience and expertise should complement each other.
- More capital may be available than in the case of a sole trading enterprise.
- A partnership does not have to pay corporation tax but needs to file a Return of Income with the Revenue Commissioner every year, under the self-assessment system.

Disadvantages

- Partners may turn out to be incompatible; therefore it is advisable to draw up a Partnership Agreement, incorporating shareholding, how difficulties should be managed and break-up clauses.
- If liability is unlimited, partners may be personally liable for the debts of the business.
- The death or bankruptcy of a partner dissolves the partnership
- In the event the partnership runs into financial difficulty, each partner is equally personally liable for all the debts of the business.
- Currently post Celtic Tiger a large number of individuals are highly indebted and in order to get a Tax Clearance Certificate for the partnership, each of the partners have to be tax complient.

Other forms of business are:

5. Unlimited Companies, have the all same benefits as a company except the directors remain personally liable for the debts. At first it may appear as the worst of both worlds, in reality business people go for this option where there is significant share holding and the owners want to minimise the amount of information they have to file in the Companies Office for public knowledge

6. PLC's A public limited company has more than 7 members and shares are traded on the stock market. There is more information available on all PLC's as they have to publish results every six months and a full set of accounts every year that is presented to the AGM

7. **Clubs and Associations**. Each has its own structure and it should be checked out individually and the exact legal status established before credit is granted. When dealing with this type of organisation it is a good idea to find out when their AGM is held and who the officers, and in particular who the treasurer is and how they can be contacted.

CREDIT APPLICATION FORM

Every business should have a clear credit application form. Ideally this form should be completed by the customer to give you enough information as to who they are and how they wish to be served. In reality if your company has field sales staff, they should complete the form with the customer. Your application form is the basis of all future contact with your customer and make sure that at the outset that you ask the correct questions.

Your New Account Application form should:

(a) Give you enough information so you can be happy you can trust them for the required amount
(b) Tell you about their requirements and how to serve them the way they want to be served?
(c) Be signed by the customer to show they have accepted your terms and conditions including Retention of Title if applicable.

Request for credit generally begins with the completion of a Credit Application. This information in most cases is procured by the Sales Representative for the Credit department to make decisions in setting the credit terms and conditions. It is a direct source of information and its quality and dependability is directly proportional to the quality of interview with the subject. The application also extends the information gathering process by seeking the applicant's Bank and other Trade references. The application can also request financial statements. Financial statements can contain inaccuracies or questionable information but it also helps in corroborating information provided by the applicant on the credit application or through the Sales representative.

Generally all the accounts should be opened after receiving and evaluating a satisfactory Credit Application. A well-reviewed account will help save valuable time in attempting to either collect or enforce in the event of a default.

A Credit Application serves the following purposes:

- It is an information gathering tool
- It is an assessment tool to determine amount and duration of credit
- It is a collection tool
- It is a legal document that binds the applicant to your terms and conditions
- It is an enforcement tool
- It is a monitoring tool. Revisit the credit applications of your important customers
- It is a marketing tool that markets your loan. In essence a 'loan application'

If you are in the process of designing a credit application or reviewing your existing one, then here are the important issues to consider.

- What is the information that you require from the applicant for you to assess the credit worthiness after supplementing it with other credit information resources like a credit report?
- What are the terms and conditions of credit and sales that you want the applicant to adhere to?
- What are the legal disclaimers that you would require to conduct the credit investigation?

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Does the customer find the process simple and easy to comprehend and at the same time understands why the information is required?

As a commercial creditor here is a list of factors that would require attention in drafting a Credit Application:

1. **Legal Name**: Ask for the legal name of the applicant first on your Credit Application and then ask for the 'Trade style' or 'doing business as'. The company can operate under different Trade names but will have only one 'Legal' name. Thus it is important to sign-up the company with its legal name.

2. **Type of Business and Industry:** Which industry does the applicant belong to and whether the applicant is in a) Retail b) Service c) Wholesale d) Manufacturing this information will help in evaluating the risk that you are dealing with. Typically there are a lot more business failures in a particular industry and especially in the area of Retail and Service.

3. **Type of Product or service the applicant supplies:** This will also help in determining if the applicant's products will compliment and supplement the product or product line that the applicant is seeking to purchase from your company.

4. **Style of Business:** Whether the business is a a) Sole Proprietorship b) Partnership c) Limited liability Corporation. In the case of a Sole Proprietorship and partnership the liability extends to the individuals running the business and thus it becomes important that the personal information of the principals along with their full names, home address and telephone numbers are sought on the credit application.

5. **Number of employees:**

6. **Estimated Annual Sales:** Number of Employees and Estimated Annual Sales not only gives an idea of the size of the applicant but also helps evaluate the 'sales to employee' ratio that would indicate if they are over or underemployed.

7. **Number of years in this business:** It is important to ask 'in this business'. Obvious reasons being that the applicant could have in business for a long time but could have only recently started this or the current business.

8. **Bank Reference:** Ask for a 'borrowing account'. Get the account numbers and also the Account Manager's name. Some even insist on a copy of a void cheque. This helps in a round about way to substantiate the company's legal name.

9. **Trade References:** We recommend that four references are asked for. However, asking for more than that could further test the credit worthiness of your applicant. If possible ask for one Trade reference from your industry. This could indicate if

the applicant is coming to your company after having short changed another from your industry. Make sure the level of credit extended by the references is a significant amount for the business. A company with a multimillion turnover who give you references that account for a few thousand in purchases in a month could indicate they do not have a good track record with their main suppliers.

10. **Web site URL and Email address:** Email address is a vital tool of communicating and can aid quick collection and transfer of documents especially when a customer claims that they have not received the invoice. Remember always that they write their own websites and the information is designed to paint themselves in the best possible light. Multiple email contact details are also important, you should get as many relevant people who will interact with your company as possible from the buyer to the accounts payable person.

11. **Signing officers and accounts payable contacts**: email, direct telephone numbers and fax numbers.

12. **Authorized Signature:** The credit application should be signed by someone who is authorized to do so. It should then bear the person's title the date and place.

13. **Terms and Conditions:** The credit application should bear the terms and conditions of sale that are detachable and a copy given to the customer at the time, printing your terms & conditions on the back of the form that is returned to your office is not a good idea!

14. **Disclaimers:** Some of the important considerations in writing your disclaimers would be as follows:
a. Permission to do a check with the applicant's bank/financial institution and trade references not just at the time of setting up of the account but from time to time.
b. If you need to check the personal credit history of any individual or principal then you would require their permission in writing. If you are making provisions for 'Personal Guarantee' then make sure that your state/provincial laws do not require that to be notarized and as a separate addendum.
c. Statement that upon signing the information that has been provided is certified to be true and correct and that it will be used and based to make the credit decision.
d. The applicant will be bound by the terms and conditions on the Credit Application whether on the front or reverse.
e. That a faxed application will be deemed as original
f. A statement of interest to be charged. Certain jurisdictions might require this as a separate addendum. The allowable rate could also vary. From an EU perspective in all business to business transactions you are entitled to charge 8% above the ECB base lending rate on all overdue accounts without

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specifying in your terms & conditions as it is the law.
g. Discounts and the definition of overdue. Discounts and payable dates.
h. Statement that no oral agreements or modifications will be accepted.
i. Statement that in the event of dispute the laws of which state would apply and in which state would be the forum for the court proceedings.
j. A statement whether legal fees or collection cost will be added on to collect overdue accounts.

Your legal people should review the final draft of your credit application.

The following form can be used as the basis of your Trade Application form:

Insert Your Logo Here

Insert your Companies Name, Address, Accounts Phone Number, eMail address, website Fax No

New Customer Information

Trading Name ____

Legal Name (If different from above)____

Trading Address____

Delivery Address(If different from above)______________________________________

Tel No__________ Fax No: _____________ Mobile _________Website www._________

Business Type:

Ltd Co ☐ Sole Trader ☐ Partnership ☐ Subsidiary* ☐ Government ☐ Other ☐

Registered Number_________________ * Parent Company ________________________

Has the business traded under any other name in the past 3 Years?
If so Name_______
For Sole Traders & Partners

Name Home Address Date of Birth

________ _______________ ☐☐☐
____
________ ______________ ☐☐☐
____

Contact in your:
Accounts Payable Dept _______________________Direct No _________ Email_________

Purchasing Department _______________________ Direct No _________ Email________

Do you have a Purchase Order System ☐ Yes ☐ No

Invoice delivery method: Post ☐ eMail ☐ EDI ☐ Other ☐

Send Invoices to:____

Do you require statements? ☐ Yes ☐ No

We reserve the right to send statements for any outstanding balance at any time

Statement delivery method: Post ☐ eMail ☐ EDI ☐ Other ☐

Send Statements to:
____

Do you require priced delivery dockets? ☐ Yes ☐ No

If Export: VAT Number ____________________Currency: _____________________

Vat Exempt Yes _____Certificate attached _______

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Estimate of monthly purchases €_______ Estimated first Year Spend € __________

How long are you in business? _____Years ☐ Premises: ☐Owned Leased

Can you list three Companies in your business that would benefit from doing business with us?

Company Person Contact details

1. ___________________ ______________________ ______________________

2. ___________________ ______________________ ______________________

3. ___________________ _____________________ ______________________

Trade References:

Company Name Contact Phone No

1_____________________ __________________ ______________

2_____________________ __________________ ______________

3_____________________ __________________ ______________

4_____________________ __________________ ______________

Payment Method:

Direct Debit	Monthly Manual Cheque	Monthly Cheque Run Specify Date	Bank Transfer	Debit/Credit Card	Cash	Pay Pal

Payment Terms
____

I confirm the details given above are correct. I have received a copy of [Your Company's] Terms & Conditions which include a **Retention of Title** clause and agree to adhere to same. I will pay all amounts due on the due day as per our agreement. I/we agree that this information may be used to support a request for credit facilities with you and your associated companies in accordance with their credit vetting facilities.

Signed____________________________ Name __________________________

A duly authorised officer

Position ___________________________ Date ___________________________

Witnessed By: ______________________ Date: ___________________________

Other information included to support our application – Please specify:

Copy Sales Brochure	
Audited Accounts	
Tax Clearance Cert	
Letterhead	
List of Customers	
Testimonials	
Security offered	
Vat Exemption Form	
Other (Please specify)	

For office Use only:

CRC		CC	
DT		SPC	
VN		CAN	
CLA		CRC	
PB			
AB			
TR		TSU	

Direct Debit Mandate

To: Your Company Name and Address

Originators Identification Number

Originators Reference

1 Name and full postal address of bank & branch
____

2 Name of Account holder
____

3 Sort Code - -

4 Account Number
Banks may refuse to accept instructions to pay direct debits from some types of account

5 Your instruction to the bank and signature

- I instruct you to pay debits from my account at the request of [Your Company]
- The amounts are variable and may be debited on various dates
- I will inform the bank in writing if I wish to cancel this instruction
- I understand that if any direct debit is paid which breaks the terms of this instruction, the bank will make a refund.

Signed____

____

Date ____

DD Logo

Please charge our Company Credit Card/ Laser Card for any goods purchased ☐

Our Credit card number is:

Expiry Date____________________

Signed _________________________________

Supplied by Irish Credit Management Training, 121 Lower Baggot Street, Dublin 2

The following document explains each of the fields above - and explains why each question is asked, and why the information is useful.

The first and most important step in building excellence through credit management is to have a proper new account opening procedure.

Start with a New Account Application form that asks all the right questions to satisfy yourself that:

(d) You have enough information to be happy you can trust them for the required amount?
(e) You know enough about their requirements to serve them the way they want to be served?
(f) They have accepted your terms by signing the application?

So much effort is expended in business to get new customers. You have teams of highly paid and rewarded sales people who are measured, monitored and rewarded by the number of new accounts they open and the resultant increase in sales. Time and effort would be better spent in retaining existing customers by delivering an excellent service and seeking to build the business on the ones we like doing business with.

Customers tend to do business with suppliers they like and feel as if they are cared about. We must demonstrate our care for our customers at every opportunity and the very best place to start is at the very beginning when the customer agrees to do business with you.

Taking a name and delivery address along with the details of the order alone may be enough to deliver the first order – you should be aspiring to do far better business with every customer than just one order!

There are questions you need answered for two reasons:

(a) Do you want to do business with them?
(b) How can you serve them better?

For the purpose of this section you really need to know who your customer is – if this sounds obvious ask your Credit team if they have ever received a cheque or payment with a different name than appears on your account information.

If the answer is yes – you have a problem because you don't know who your customer is. Is it the person you are invoicing or the person that is paying?

If the answer is no – you could have a bigger problem. Ask to see copies of the cheques and payment advises for one week, (best pick the last week of the month when most payments come in) and a copy of the debtors' ledger and check it for yourself.

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This exercise alone could save you thousands as 60% of accounts passed to legal firms for collection fail or are delayed because the supplier does not know who their customer is.

It can also be the cause of delayed payments near the end of a company's life cycle as if you have demonstrated sloppiness by having their contact details wrong you will be put at the end of the line.
This is just as relevant for small and multinational companies – with small businesses you must ensure you have the correct legal entity and not just a trading name. For multinationals you must ensure you have the correct trading division.

Now that you are convinced of the need for such a document – please go line by line through the document to select the questions that are relevant for you and discard the ones that are not applicable to your business.

New Customer Information

Title is far less threatening that Credit Application Form for Trade Customers

Trading Name _________**This must contain the name that appears over the door**___

Legal Name (If different from above)___**This should contain the name of the person or company you are doing business with and must be a person or a company or another valid legal entity.**

Trading Address___**This should contain the address where they carry out their business**

Delivery Address(If different from above)__**Where the deliveries are to be made**__

Tel No__________ Fax No: _____________ Mobile _________Website www._________

Complete with country code and area code if applicable

For info – remember they wrote this stuff!

Business Type:

Ltd Co Sole Trader Partnership Subsidiary* Government Other

The rule for business is "trust but verify" make sure this answer is consistent with "legal name" above

Registered Number________________ * Parent Company _____________________

Every Company has a unique number **See the rules – if the Company is 100% owned this will be the entity you are concerned with. If not you may need a parent company guarantee**

Has the business traded under any other name in the past 3 Years? If so Name______

Just in case you have an existing account that wouldn't link

For Sole Traders & Partners

Name Home Address Date of Birth

_______ _____________ ___________________________________ ☐☐☐

_______ ____________ ___________________________________ ☐☐☐

For sole traders and partners they are personally liable for the debts of the business. In the event of failure you need to know how and where you can contact them. Most companies write off money because the business is "gone away" with this information you will be able to follow up even if the business fails – and increase your chances of getting paid.

Contact in your:

Accounts Payable Dept ____________________Direct No ________ Email________

In business the person paying the bill must Become your best friend! Right from the start you must look to every opportunity of developing and growing your professional relationship

Why talk to two people for when you only want to ease talk to one? of contact

Purchasing Department ____________________ Direct No ________ Email_______

This is the person your sales and customer service people should make a point of getting to know.

Do you have a Purchase Order System ☐ Yes ☐ No

If the answer is yes – you must put in a system that ensures no work is done or no goods are delivered without a valid PO being received first.

Invoice delivery method: Post eMail EDI Other

☐ ☐ ☐ ☐

We work in the 21st century and the old snail mail has been replaced in the main with electronic methods of communication – why not extend to invoices? Ask the question.

Send Invoices to:____

If we assume we should send invoices to the trading or the delivery address we will add to delays in payment and look unprofessional. Ask the question at the start and get everything right first time

Do you require statements? ☐ Yes ☐ No

We reserve the right to send statements for any outstanding balance at any time

Most statements are put directly into the bin – ask your customer do they require them – if they do send them if they don't - don't.

Statement delivery method: Post eMail EDI Other

☐ ☐ ☐

Send Statements to:

____

Do you require priced delivery dockets? ☐ Yes ☐ No

If Export: VAT Number ___________________Currency: ____________________

Vat Exempt Yes ____Certificate attached ______

Estimate of monthly purchases €_______ Estimated first Year Spend € __________

This information is the only indication you will get as to the potential size of this account you should use these figures to establish a credit line consistent with best practice.

How long are you in business? _____Years ☐ Premises: ☐ Owned Leased

The shorter the time the higher the risk factor

More applicable to pubs, coffee Shops & Restaurants – gives you an indication of security available

Can you list three Companies in your business that would benefit from doing business with us?

Company	Person	Contact details
4. __________________	______________________	______________________
5. __________________	______________________	______________________
6. __________________	______________________	______________________

One of the more unusual questions to find on such a form. It makes great sense when you think about it. Your sales people will get these forms filled in – they know they should ask for referrals – they know they don't. This question forces them to get referrals and the possibility of gaining new customers.

Trade References:

Company Name	Contact	Phone No
1______________________	___________________	______________
2______________________	___________________	______________

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3______________________   ___________________
____
4______________________   ___________________
____

Yes 4! – most companies ask for two – and most customers can keep two suppliers paid to terms on a consistent basis. This gets much harder when you ask for four!

Payment Method:

Direct Debit	Monthly Manual Cheque	Monthly Cheque Run Specify Date	Bank Transfer	Debit/Credit Card	Cash	Pay Pal

In some instances you might tick the box in others you would ask your potential customer to do it – depending on the balance of power within the relationship. You should always ask the question when & how are you going to pay – right at the very start, if nothing else it proves that getting paid is important to you.

Payment Terms
____

I confirm the details given above are correct. I have received a copy of [Your Company's] Terms & Conditions which include a **Retention of Title** clause and agree to adhere to same. I will pay all amounts due on the due day as per our agreement. I/we agree that this information may be used to support a request for credit facilities with you and your associated companies in accordance with their credit vetting facilities.

Signed_____________________________ Name ___________________________
A duly authorised officer
Position ____________________________ Date ____________________________

Witnessed By: _______________________ Date: ____________________________

Other information included to support our application – Please specify:

Copy Sales Brochure ☐
Audited Accounts ☐

For office Use only:

CRC		CC	
DT		SPC	
VN		CTA	

Tax Clearance Cert	
Letterhead	
List of Customers	
Testimonials	
Security offered	
Vat Exemption Form	
Other (Please specify)	

Suggested codes for "office use"

CRC= Credit References checked

CC = Credit Controller responsible for this account

DT = Depot

SPC= any special price agreements or groups

VN = the van or delivery route associated with this customer

CTA= Terms agreed

TRA= Trade references attached

RC=Risk Category

PB = Proposed by – usually the sales person

AB= Approved by – usually Credit or Finance

TR= time & date received

TSU= time and date the account was set up

Direct Debit Mandate

Is mostly self explanatory

Originators Identification Number is the account number or reference you require to be able to identify your customer.

Originators Reference is your unique authorisation from your bank to be able to take Direct Debits.

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Correct DD Logo – must appear on all documents

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So much effort is expended in business to get new customers. You have teams of highly paid and rewarded sales people who are measured, monitored and rewarded by the number of new accounts they open and the resultant increase in sales. Time and effort would be better spent in retaining existing customers by delivering an excellent service and seeking to build the business on the ones we like doing business with.

Customers tend to do business with suppliers they like and feel as if they are cared about. We must demonstrate our care for our customers at every opportunity and the very best place to start is at the very beginning when the customer agrees to do business with you.

Taking a name and delivery address along with the details of the order alone may be enough to deliver the first order – you should be aspiring to do far better business with every customer than just one order!

There are two key questions you need answered:

(c) Do you want to do business with them?
(d) How can you serve them better?

For the purpose of this section you really need to know who your customer is – if this sounds obvious ask your Credit team if you ever receive cheques or payment with a different name than appears on your account information?

If the answer is yes – you have a problem because you don't know who your customer is. Is it the person you are invoicing or the person that is paying?

If the answer is no – you could have a bigger problem. Ask to see copies of the cheques and payment advices for one week, (best pick the last week of the month when most payments come in) and a copy of the debtors' ledger and check it for yourself.

This exercise alone could save you thousands as 60% of accounts passed to legal firms for collection fail or are delayed because the supplier does not know who their customer is.

It can also be the cause of delayed payments near the end of a company's life cycle as if you have demonstrated sloppiness by having their contact details wrong you will be put at the end of the line.

This is just as relevant for small and multinational companies – with small businesses you must ensure you have the correct legal entity and not just a trading name For multinationals you must ensure you have the correct trading division.

If you are dealing directly with consumers there is a completely different form and a different set of information you will need to help you make a decision on granting credit. The following form covers the main information you should ask for. This application form should be completed for every single transaction or new loan the consumer takes out with you.

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Your Consumer Credit Application Form

Account Number

Credit/ Loan Application Form

Contact Details
Mr ☐ Mr☐ M☐ ☐her ___________Date of Birth: ___________________
First Name_______________________ Surname_____________________________________ Current Address ____ ____ ________________

Contact Details;
Telephone Home____________________ Work _________________
Mobile _______________

Marital Status ☐ Single ☐ Married ☐ Separated ☐ ☐
Widowed Co Habiting

Number of dependants (Excluding spouse/ ☐)

Residential Status At home with parents Tenant Home owner

How long at this address _________________ ☐ ☐ ☐

Previous addresses if less than 5 years:
(1)______________________________No Years__

(2)______________________________No Years__

(3)______________________________No Years__

Residential Status of last previous Addresses:
At home with pare☐ T☐ant H☐ne owner ☐ Mortgage

Name of Partner/ Name of
spouse____

Employment Details

Employed ☐ Self Employ ☐ Homemake ☐ ☐
Unemployed

Name of Employer
____

Address of Employer
____

Position _______________________________ No Years Service
____

Previous details – if less than three years
Name of Employer
____

Address of Employer
____

Position _______________________________ No Years Service
____

Bank
Credit Card Visa	Mastercar	Other (please specify)
____

Ongoing Commitments:		
Owing	Monthly Cost	Amount
Mortgage/ Rent		
Car Loan		
Credit Cards		
Overdraft		
Other Loans (including Moneylenders)		
Store Cards/ Mail Order		
Childcare Costs		
Maintenance		
Other Credit Union		
Total		

Mortgage Provider
____

Income Details

Weekly/ Monthly take home pay	€___________	Spouse
€_______________
Other Income	€ ____________Spouse €
____

Loan Details

Amount Applied For €_________________	Term of Loan:
____

Purpose of Loan ___________________________________Loan Number:
____

Repayments Amount: € __________________(Includes/ does not include RPI see below)

Weekly	Monthly	Lump Sum	Other	Specify ____________
☐	☐	☐	☐	

Repayment Method:

Standing Order	Direct Debit	Personal Lodgement	Other
☐	☐	☐	☐

If Other – please specify: ____

Repayment Protection Insurance (RPI)

The benefits of repayment protection Insurance have been explained to me and:

I Wish to protect the repayments and have received the policy documents Signed	I understand my repayments are not protected Signed

I declare I am not indebted to any other Credit Union, Bank or Loan Agency either as borrower or guarantor, except as stated above. The statements made herein are made for the purposes of obtaining a loan and are true to the best of my knowledge and belief. I also hereby authorise you to make whatever enquiries that are deemed necessary to process this application including sharing account and loan data, with other agencies

Signature of Applicant_________________________________ Date ____________________

Joint Account only:

Signature of Applicant_________________________________ Date ____________________

For Office Use

Supporting Documentation

Year Account Opened ____

Account Status currently ____

Loan to Shares Ratio ___________: (for Credit Unions)

% Disposable income to debt repayment: _________________%

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Savings History ____

Previous Loan History ____

If employed:

Pay Slips	☐
Last three months Bank Statements	☐
P 60	☐

If self employed:

Full set of Accounts	☐
Tax Clearance Certificate	☐
Revenue Notice of Assessment	☐
Last three months bank statements	☐

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Form of Security

Savings

Guarantor

Letter Of Undertaking

Title Deeds

Other (Please Specify)

____

Proposed Guarantor Name
____

Address
____

Occupation
____

Contact Number ______________________ CU Account No
____

Standing Order Signed Direct Debit Signed

____

Guidelines for completing the Loan Application Form.

Personal Details

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Existing information on file for the member must be verified before being put into this form.

This form should be updated here there are gaps or information to be updated.

Mr, Mrs or Miss – Tick Box. Other is for Dr, Fr, Bro. Etc

Full Name – as it appears on the photographic ID – If they are known as a different name than the one on the ID – this name should be in brackets after their first name.

Address is where they are currently living

Previous address – helps you get Credit history

Ask for all three phone numbers

Marital Status _ tick relevant box

Number of dependants – include all children and dependents living in the home and other dependants from previous relationships

Residential Status – this refers to the current address

Full name of partner and first name and maiden name of spouse – if applicable – this is an optional field.

Employment details

Tick Box for status – if they are on Contract or Consultancy – tick Self employed box.

Name of employer – if self enter – “Self”

RTCC – Recommendations to Credit Committee – Yes , No or If… (for Credit Unions etc)

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D***isclaimer***

This form is supplied to assist you to ask the correct questions when making a credit decision and as such is for information purposes only. It does not constitute legal advice and should be approved by your legal advisors prior to use. Laws are constantly changing and what you can and can't base a credit decision on changes from time to time.

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Trade References

Trade References are a great source of information. You should ask for **four** as per the new customer information sheet. Some companies request information in writing. It is far easier to pick up the phone, talk to the appropriate person and ask the following questions in a friendly manner:

Trade Reference Questionnaire

Subject ____

Company Contacted ____________________________________

Contact Person ______________________________________

Phone No ____

Date ____

How long do you know them? _____________________________

Approximate amount of Credit Extended €___________________

Credit Terms ____

Do they pay to terms? __________________________________

Anything else I should know? ____________________________

These forms should be kept on file with the new customer information sheets for future reference.

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Trade References

Trade references are normally obtained on your credit application and checked at the time of setting up of a new customer/applicant.

It is a good practice to check references even at a time when an established customer starts to show signs of financial stress or changes their buying or payment pattern. A periodic check on trade references is recommended on customers those contribute to the cash flow of your organization. Do not be surprised if you uncover something unexpectedly! Moreover it also shows that you care about your exposure and that you monitor it regularly.

The following is a checklist of things to ask and look for while checking the reference provided by the applicant for credit.

1. Number:

   It is recommended practice to ask for four (4) trade references on a Credit Application. Over the ages companies have looked for two this has taught the average customer looking for credit to walk around with their best two references while applying for credit. What if as creditors we ask for four or more. It is a subtle way of forcing the applicant to look for and supply you with one or two more suppliers with whom they have a healthy business relationship.

2. Primary Versus Secondary Supplier:

Find out if the reference provided is a primary or secondary supplier to the applicant. Generally we tend to give preferential treatment to our Primary suppliers on which our business depends. Thus we also end up paying them first. Checking whether the reference is a primary or secondary supplier to the applicant might help reduce that particular anomaly.

3. At least one trade reference from the industry:

   Ask for at least one reference from your industry. It will help you in ascertaining whether they have abandoned one to now join the other, the other perhaps being you.

4. Location of the Trade Reference:

Again local suppliers tend to get paid first. Finding out the location of the trade reference could provide some insight into the payment practices of the applicant.

5. Date Opened:

   Try and ask for trade references where the applicant has had trade dealings for at least one to two years.

6. Related Party transactions:

   Find out if the references provided are related parties. You might be getting a biased reference. Also, upon insolvency 'related party transactions' are viewed as 'non-arms length' transactions. The remedies for these transactions are worth investigating.

7. What References were provided to the Trade References by the applicant:

When speaking to one or more of the references provided to you on the credit application try finding out the trade references that were provided to these references by the applicant, at the time that the applicant filled an application for credit with these trade references. Then call these references. This will perhaps give you a more meaningful insight into the payment habit of the applicant.

8. High and Low credit in the past 12 months:

   The amount given as high credit to the applicant displays the exposure and confidence that the supplier had in the applicant. The figures can also be used to judge and set your own limit with the applicant. If the amount of credit sought by the applicant is significantly higher than the amount indicated by the references then perhaps you might want to proceed with caution and the case might warrant further investigation.

9. Amount Current:

   This amount would especially be of significance and concern if during the peak season of the applicant the amount current were relatively low. This implies that you should also know the business cycle of the applicant to aid your analysis.

10. Amount overdue:

    This will trend the payment habit of the applicant and give you a rough aging analysis against the terms as discussed next.

11. Terms:

Find out if the applicant has any special terms with the references provided. Also, find out if the reference gives any special discounts like 2%10 Net 30. If so, then does the applicant avail of such discounts or abuses it by taking the discount and still paying late.

12 General Payment experience:
How has the payment relationship been over the period of their business partnership? Slow 30, Slow 45, Slow 60 …satisfactory, unsatisfactory excellent etc might be some of the typical responses.
13. Length of time sold:
This would indicate the duration of the relation ship of the applicant with the reference that you are checking.
14. Last Sale:
It is important to know if the applicant is a regular customer of this Trade reference that is provided to you. It could be just a one time or a short and sweet relationship that the applicant had with this supplier.
Other Avenues:
15. The Golden Pages:
Study the 'heading' under which your applicant is listed in the Golden Pages and then call some of the others listed under the same heading to find out more about the applicant. This will be of special value if the customer is out of town or even in a different country.
Note: Golden Pages & Yellow Pages are now available online.

16. Credit Group/Association meetings/ Credit Circles:
Valuable information regarding the credit worthiness of the applicant can be picked up at Credit Group meetings.
Just as a tip, if you were checking references other than the ones that were provided to you on the credit application a good *disclaimer* on your credit application would address that condition. A disclaimer that would indicate that, you will be able to check the references provided to you on the credit application and others that become available to you or you become aware of during the credit review process and from time to time. A good idea would be to review your disclaimers on your credit application in light of the above with your legal dept.

Thus, trade references help in analysing the applicant. It also aids in setting limits and determining your exposure. Trade references are another avenue to monitor accounts during the course of your business journey with them. It all depends on how creative you are in using this valuable resource of credit analysis.

Another benefit of using trade references is that you are accessing real time information, as opposed to the information available in the CRO that can be up to two years old.

Available information

Information is available from:

- Your own systems.
- Your own sales and operations staff.
- Companies in a similar business in the trade
- Reference agencies.
    - D&B www.dnb.co.uk
    - Experian www.experian.ie
    - Credit Safe www.creditsafe.ie
    - Bureau van Dijk www.bvdep.com/en/
    - Vision Net www.vision-net.ie/
    - Checkit www.solocheck.ie/
    - Search4less www.search4less.ie
- Judgment searches –
- Stubbs http://www.stubbsgazette.ie
- Experian www.experian.ie

Available Information (Contd)

- Companies registration office. www.cro.ie

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- The Irish Times
  www.irishtimes.com
- International information www.FT.com
- Credit insurance companies.
  - Atradius www.atradius.com
    - Where you can download free country reports
  - Coface www.coface.com
  - Euler Hermes www.eulerhermes.com
- Irish Credit Management Training www.icmt.ie
- Contacts in Professional Associations like the Irish Association of Credit Professionals. www.youracp.org

How much can I trust them with?
Stress Tests.

In accounting speak, this is often referred to as a credit limit; I would prefer to call it a credit facility or a line of credit or a credit line. Either way, you really should set out at the beginning how much credit you are prepared to extend to each customer. This should act as a guide: at no stage should it be written in stone and lines of credit should be reviewed regularly, in line with seasonal and other business trends in addition to their changing status based on the level of business and the profitability of the business you are doing with them.

Like most elements in credit management, setting lines of credit is a combination of art and science. There are seasoned credit professionals that have used and relied merely upon their gut feeling to grant credit limits. However, it is always better to take a 'calculated' risk than base your decision purely on gut feeling, although combining the two can be the best method of all.

Credit Limits helps the creditor in the following ways:

1. It frees up valuable time for other credit management tasks
2. It speeds up the sales process
3. It reduces risk and improves collection activity and efforts.
4. It is an account monitoring tool

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Credit limits have also known to upset customers. Thus, the decision to communicate credit limits to your customers rests upon you. It has its advantages and disadvantages.

One important approach that credit management should take with customers who are near their limits, this is the time to collect more information on your customer or cajole them into paying overdue amounts. Credit Limits need not be Sales Limits and should be used as a guide to enhancing profitable sales. They should be flexible and revised often.

Issues to consider when setting Lines of Credit

The first thing that the company needs to consider is its own exposure. What is the kind of exposure that a company can take with its customer base? Will it be a Liberal or a 'Conservative'?

Important factors influencing these elements will be

- The strength or weakness of 'Product or Service' that is being sold;
- The degree of 'Competition' or 'Opportunities' in the marketplace; the nature of the industry that you are in or deal with- Is the industry growing or going? Your role as a supplier, especially if you are the key supplier to your customer.
- Whether you are a 'Secured' or 'Unsecured' creditor. If there is any lien rights that you can obtain or exercise.
- The financial strength of your customer; the information that you have or can obtain from your customer or other sources.
- The number of years that the customer has successfully run that particular business
- Their reputation in the marketplace, both of the business and its directors and management.
- The customer's businesses plan or blueprint to operating the business in the future
- In difficult times when long term planning is difficult if not impossible, their ability to achieve and exceed quarterly cash flow targets can be used as a measure of their ability.
- The overall 'Margin' that the product or service contributes to the bottom line;

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- The confidence that you have in your in-house ‘Collection’ process;
- The length of your terms to your customer because risk is directly proportional to the length of your terms

Another vital question that senior management in the company need to answer is: How much of their working capital are they willing to employ in their customers? Often companies forget to first evaluate these questions and get themselves into a cash crunch situation.

Methods of Setting Credit Limits

As indicated earlier setting credit lines is not a science. Although, by incorporating the process into their scoring models some companies have made it into a near science. The starting point to setting most credit limits is the needs and requirements of the customer. What is the customer asking for and subsequently what will be the requirement periodically? If the customer is creditworthy then would you as a customer want to set the a credit limit for the customer higher than what is being sought in order to save time in the future i.e. if credit lines are to be increased later due to increased sales volume?

The following are some common techniques applied in setting Credit Lines:

Trade References: After obtaining the trade references you can compare the amounts of the High Credits awarded to your customer.(applicant) You can choose the ‘Highest’ from the ‘High Credits’ or take an ‘Average’ or pick the ‘Lowest’.

Bank References: In doing a bank reference on your applicant find out the amount of line of Credit that was established by the applicant with the bank. If this line is unsecured then perhaps it can give you a little more comfort in setting a relatively higher credit limit for the applicant. The use of this information is rather sketchy since the banks generally are secured creditors with stiff remedies upon default.

Agency Credit Reports: Credit Agencies generally give two pieces of information that are quite popular among credit professionals that aid in the setting of credit limits.

1. Payment Performance: This section lists the paying habits of the applicant. The information is collected from different suppliers to the applicant. You can treat this section almost like doing a

trade reference. It will give you High Credits and the customer's (applicant) payment habit in different dollar ranges. It is quite possible that the customer might be a good paymaster in the dollar range that is being sought from you as a credit limit. Thus, increasing your confidence level.

2. The Rating: Based on certain credit and financial information obtained on the customer (your applicant), the Agencies assign ratings. These ratings can assist you in setting your own credit lines. You can map your own credit line values against individual ratings that a credit agency assigns. Be careful in applying agencies recommendations as a sole source of information. At best the information is between one and two years old for larger credit lines you must conduct your own verification processes, which we will deal with later.

Financial Statements: Financial statements are also used in assigning Credit Lines to customers. Mainly ratios or factors like net worth and working capital are taken and trended or compared to Industry norms or standards. If a customer shows liquidity and efficiency as per industry norms then a more confident approach can be taken in setting the credit limits. One has to also consider if short-term liquidity is important or meaningful to the nature of your credit or is long-term liquidity more consequential.

For Example: Some companies will take the 'Tangible Net worth' [Total tangible assets – Total liabilities. From the Balance Sheet] and assign anywhere between 5% to 15% of the Tangible Net worth as a credit limit for the customer provided the customer has shown pre-tax profits. Others consider Net Working Capital [Current Assets-Currents Liabilities] because it measures the short-term liquidity of a company. While doing such analysis one has to also consider elements outside the domain of the financial statements before making a conclusive decision. For example the company that is being assessed might have judgments registered against them. On the other hand the financial statements could be unaudited.

Another ratio that is of importance to lenders is the 'Debt to Equity Ratio'. The ratio is typically calculated by combining noted payables and all secured debt (such as short term and long term bank loans and debentures) and dividing it by net worth. The ratio shows how the company is leveraged and illustrates the stake of the lenders as opposed to the owners. A secured creditor (like a bank) may request to maintain a certain level of Debt to Equity. Otherwise upon default such loans become payable upon demand, which could lead to sale of assets to prepayment of the loan. If this ratio is within industry norms and to the satisfaction of the secured lender then a more liberal approach can be taken in setting the credit limit for this customer. The contribution to the credit limit can range anywhere from –5% to 15% of the customer's Net Worth.

The Days Sales Outstanding also known as D.S.O is a rough indication of the quality of a company's receivables. It is calculated by dividing the net receivables by average daily sales. If the DSO is in line with the norms for the industry then a liberal approach can be taken in setting the limit for this customer. The formula that is used with DSO is that, for each day of deviation from the norm or the selling terms you add or subtract .10% of the Net Worth.

Past Performance: Credit Lines in this case are based on the past history of the customer as per the information contained in your books. The two elements that you would consider and weigh would be the past:

- Payment performance
- Purchase Pattern

Need Based: In this case Credit Lines are set based on the needs of the customer. It could be set to accommodate the first *Requested Credit Limit or* the *Size of the first Order:* It should not be done in isolation but by a combination of the other methods that are discussed here.

One of the most popular techniques used for setting credit lines is by using the information and ratings given by credit agencies.

How long can I trust them for?

In accounting speak, this is often referred to as credit terms; we will deal with this topic in more detail in the next section. You must resolve that your credit terms are clear, enforceable and consistent with doing business.

Overall approach

The purpose of your credit assessment procedure must always be to find a way to deliver every order. Some companies, in difficult economic times spend more time qualifying potential customers, and looking to create barriers than to doing business. While it is understandable that business has to become more cautious in more difficult times, it is equally important that we capitalise on all available profitable sales. While it is not always possible to give every customer all the credit they may be looking for, it is always possible to deliver the next order.

You should also make sure you are giving credit for the right reasons. The only reason to give credit is if it helps you to sell more. If a customer is willing to buy your product or service and pay upfront - Take the money!

Summary Credit Risk Assessment

- Do I trust them?
- Did the business make a profit or loss over the most recent period?
- Is their business getting better or worse?
- If worse – is it better or worse than the underlying trend in the industry?
- What does the business own and owe at the end of the period
- What is their cash flow & availability of funds
- What is the outlook for their sector

In the current climate most companies are coming out of a long period of posting losses and traditional scoring models weren't built to cope with this. If your customer has posted losses in a previous financial year there are two things you must do.

1. Calculate the losses as a percentage of their net worth to establish its significance. If the losses are 1% of net worth this may not be detrimental to the company irrespective of the amount.
2. If last years losses exceed 50% of the net worth in the business this means that another year like that will wipe them out. Getting up to date financial information in this instance is advisable, particularly if you have a significant exposure.

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Setting and Operating Lines of Credit.

Once the above information is to hand a decision should be made to advance credit or not. If a decision is made to advance credit:

(i) Decide on exact amount – this could be three times the amount of monthly credit required, it could be the recommended line suggested by an information provider or even a multiple of it. E.g. you could say for your business you are prepared to extend double what your agency recommends, you should also decide on your exact terms and apply them to the account as well. There is a full section in Terms & Conditions that deals with this area.

(ii) Record decision on your accounts system to ensure a warning is received if orders are placed for any account outside these terms and appropriate action noted in your Credit Policy. This area could be glossed over – it is VERY important. I have seen some systems that only calculate exposure on the basis of invoiced sales and do not take the orders in the system into account. Make sure you check how your system works or you might be in for a very unpleasant surprise.

(iii) Set date for a review.

(iv) Advise customer in writing

On this fourth point, it is a great idea to write to your customer as soon as the account is open to welcome them as customers and set out your terms and contact information to begin building a business relationship as soon as possible. The following welcome letter can be amended to suit your needs:

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Sample Welcome Letter

To “Contact in Accounts Department”
Your new customer
Address

Dear [first name]

Your new account has just been opened and we look forward to doing business with you. My name is [insert your full name] and I will be looking after your account.

Your invoices will be sent to [insert “invoice to address”], we understand you have/ have not got a purchase order system in place and I will ensure your requirements are complied with at this end.

We pride ourselves on the accuracy, timeliness and clarity of our invoicing, should you have any issues or require any additional information to make your job easier please let me know on my direct line which is [your direct line number as they will have to dial it] and I will do everything I can to help.

Our credit terms are [state clearly your credit terms clearly stating the exact date payments are due], and we look forward to receiving your payment each month on or before that date.

In response to your request we are delighted to extend to you a line of credit of €________ [state amount], should you wish to revise this facility, at any time, please let me know.

I look forward to being of service to you.

Yours sincerely,

____
Your Name
Your title

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Credit Assessment

Credit assessment is a topic that can be covered in 10 minutes or 10 days, depending on the level you looking to achieve. For the purpose of this module we will look at the topic in an overall sense and cover the non-financial factors, when it comes to ratio analysis and credit scoring and detailed accounts analysis, that is covered in the Risk Assessment subject as part of the overall Certificate.

Before you take on any new customer or increase exposure to an existing customer, you must be satisfied that they are willing and able to pay their bills as they fall due. Use all the information sources available to you, communicate clearly with your customer, let them know of any concerns you have and as always find a way to deliver every order.

You should consider incorporating some of the following procedures into your regular routine.

1. Comprehensive credit application form.
2. Regular review of outstanding balances.
3. Regular review of payment patterns.
4. Ongoing verification of legal entity.
5. Subscribe to payment performance.
6. Systematic review of your customers.
7. Credit insurance.
8. Personal guarantee.
9. Bank guarantee.
10. Parent company guarantee
11. lines of credit extended
12. fast-growing accounts.
13. New accounts.
14. Businesses going into their fourth year.
15. Reviews of accounts in particular industries.
16. Customer visits

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Ten Things You should do:

1. Proper New account application form
2. Communicate your Credit line & terms
3. Categorise in a risk category
4. Check out Trade References
5. Get a bank reference
6. Get most up to date information
7. Talk to others
8. Decide if security is appropriate
9. Set up all information correctly
10. Have a clear review system & procedure

- Assessing Existing Accounts
  - Payment pattern – see below for an example
  - Purchasing pattern – if purchases suddenly increase – ask the question why. Are your sales people wonderful and have secured a major contract or has another supplier put them on stop supply?
  - Query levels – If you see a sudden increase in query levels it could mean that your own attention to detail has slipped and has to be addressed or if the queries are not valid it could be a delaying tactic being employed by your customer to mask a serious cash flow problem.
  - Cheque numbers – if you keep a copy of the cheques on file you can establish the number of cheques they are writing every month. If that number has reduced dramatically they could have switched to electronic payments of they could be holding out on paying other suppliers.

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Overtrading is one of the major causes for business failure. It happens when a business over extends itself beyond its available resources. If there is a sudden increase in buying followed by one or more of the following:

- Can't pay you until they get paid
- Leaning on the trade
- Increased Sales + Reduced margin
- Reduction in Working Capital
- Dropping Current Ratio
- Depleted reserves

This is the first signs of trouble you will find it will be closely followed by:

Danger Signs

- Payment performance
- Bounced cheques
- Lifestyle
- Hard to contact
- Rumours in the trade
- Redundancies
- Attitude of Accounts staff
- Inside information

Remember

- The figures only tell half the story
- Accounts can be made to say whatever you want
- Create a jig saw of credit assessment tools
- Use your Instinct
- You only make money on Sales Paid

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Assessing Existing Customers

A snapshot of a ledger one month after another:

July 11	Balance	Current	1 month	2 Month +
Best Bet	450.00	450.00		
John Glynn	976.00	456.00	520.00	
Zephyr	1,236.00	798.00	438.00	

August 11	Balance	Current	1 month	2 Month +
Best Bet	480.00	480.00		
John Glynn	987.00	531.00	456.00	
Zephyr	2,046.00	1,248.00	798.00	

Looks pretty normal and unspectacular on the surface. Our credit terms are that payment is due on the 28th day of the month following invoice i.e. June invoices are due to be paid on the 28th July. In both months "Glynn's" and "Zephyr's" were overdue when we printed our report. In fact we would see the exact same thing if we looked back on our aged debtors for the past twelve months.

Lets look a little closer at these two customers payment performance over the past twelve months:

July	3rd September	30th August
August	3rd October	1st October
September	3rd November	3rd November
October	3rd December	4th December
November	4th January	6th January
December	3rd February	8th February
January	3rd March	10th March
February	2nd April	12th April
March	3rd May	14th May
April	3rd June	20th June
May	3rd July	23rd July
June	4th August	26th August
July	3rd September	30th September

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With this analysis it is simple to see that while both accounts look the same on an overall level, as soon as you look a little closer a completely different picture emerges. We see that Glynn's always pay us on the third of the month – they are late but consistent – we have two choices 1. ask them to pay three days earlier to comply with our terms or if they have been long standing, good and profitable customers we could adjust our terms to the third day of the second month – to recognise their loyalty and consistency, while making sure the situation remains as is.

When we look at Zephyr we see a totally different picture. For the first four months they paid on the last day of the month without fail. Then into the new year payments started to get a little late and as each month passed the payments have got later and later, to the point where they are now taking in effect a full month extra.

Like everything to do with Risk Assessment there are two possible causes for this:

They are finding it harder and harder to get the money together every month or they are pushing the boundaries to see how much they can get away with.

Export Credit Risks

If you are exporting you have exactly the same risks as the domestic market and then some more.

Currency

Be careful what currency you are doing business in. If you opt for a different currency than Euro you will have an exposure to the extent that currencies can move up and down. Depending on the level and the direction of the movement you can make more money or have your margin wiped out completely. It is good practice to contract in local currency as it removes a layer of risk. You could also open a foreign currency account in the country your customers reside to minimise your risk, as you only gain or lose money when you convert from one currency to another.

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Time Factor

Because of the sheer distances you are dealing with it can cause additional exposure. A delivery sent to Japan on a COD basis could take over 6 weeks for the goods to get there, in the meantime your own cash flow is suffering. Make sure you factor in time as a possible additional cost of doing business abroad.

Culture

You must really take time out to get to know your market. People tend to be the same the world over, this is true. There are customs and practices, religious festivals and holidays and other things that if you are talking to different people around the world you really should know. Make sure you never get caught out.

Time Zones

America is between five and ten hours behind us. Asia are four to ten ahead. If dealing in foreign markets be sure you are conscious of the time there and, if necessary, adjust your own hours accordingly. Learn when the holidays are on in your customers country and take note of them.

Communications

Words mean different things in different countries – Opel thought that Nova was a good name for a small car – no one told them that it Italy it means "won't go!" As credit management is all about excellent communications make sure you communicate cleanly and clearly with your customers everywhere.

The Five C's of Risk Assessment

What are the 4 C's of credit? What do they mean? Are there 3, 4, 5 or 6 Cs of Credit?

Credit investigation could get intricate and dense. The information that is being gathered could be getting strewn and scattered all over the place. The 4 Cs of Credit helps in making the evaluation of credit risk systematic. They provide a framework within which the information could be gathered, segregated and analyzed. It binds the information collected into 4 broad categories namely Character; Capacity; Capital and Conditions. These Cs have been extended to 5 by adding

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'Collateral', or extended to 6 by adding 'Competition' to it (Reference: Credit Management and Debt Recovery by *Bobby Rozario, Puru Grover*). How about 'Computer' being one of the Cs in this day and age?...or mere 'Common Sense'!

No matter how many Cs we come up with, the fundamental question that remains to be answered by the framework of our analysis is:
'Will I get paid on time?'

So let's discuss the structure of our credit analysis within the context of the 4 Cs of Credit

Character

JP Morgan, a successful businessman once said that 'I will do business with anyone as long as he/she is honest!'

In analyzing *Consumer Credit* one would consider the following:

- Has the person declared bankruptcy in the past
- Does the person have a good credit record
- Does he/she have a stable job
- What is the level of education/experience
- What is the person earning and what is the earning potential
- Stability at the place of residence, whether rented or owned.

In analyzing *Commercial Credit* one would consider the following:

- The size of the operations
- The number of years in business
- The legal form of the business
  o By this one means 'Retail', 'Wholesale', 'Service' or 'Manufacturing'. Typically the incidence of business failures is high in the Retail and Service segments.
  o Is the business a Parent, Subsidiary or a division
  o Does the business have a Holding company?

- The structure of the business
  o Is the business a Sole Proprietor, Partnership or Corporation?

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o For Sole proprietor or Partnership type one would further seek personal information on individual(s) running the business.

- The number of employees
  o There are Industry specific Norms for 'Employees to Sales' ratio.
- The management record of the company
- The location of the company
- Any previous evidence of fraud
- Any previous Insolvency record?
- Any Labour disputes or issues?
- Are the products/service sold by the prospect complimenting products/service to the ones that you may sell?
- Is the business practice ethical?
- Is the business seasonal/ non-seasonal
- Is the business Local/ National or International.
  o The economy of a business accordingly could depend upon local/ national or international economy.
- Is there a growing or a going market for this business or the business redefining itself and what would be the impact of the internet on this business.
  o See what computer downloads (E.g. Napster) has done to the music industry
- How willing is the prospect to share information?
- How diligently does the prospect fill your Credit Agreement/Application?
- What are the references saying?
- Are there too many lay-offs especially of key personnel?
- Are there any Law suits pending against the company?
- What does the website of the company say and look like?

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- Is there any recent media coverage about the company?
  o Is it positive or negative
  o Or are there any rumours floating?

- If the company's stock is publicly traded then see how its stock is performing?

- One can also check the indices for a particular type of Industry to see how in general the Industry is doing. The collapse of the NASDAQ last year was a warning of the debacle of the tech companies.

Capacity

What does one analyze under this segment?
Is it:
o *Capacity of the business to pay?*
o *Capacity of the business in getting paid?*
o *Capacity of the business to receive/absorb?*
o *Capacity of the credit grantor to expose?*

Sometime a business that you are analyzing might not have the required Capacity in kind but the same could be latent and hidden in some other form. For example a start-up business should have a good business blue-print of succeeding namely a good business plan. A contractor might have a good media advertising plan, say an Ad in the local Yellow Pages. All this adds to the capacity of a business to carry on trade and perhaps be successful.

Innovation, Education, Experience, Knowledge would be some other considerations. Management should be able to foresee trends in the marketplace and blend accordingly. It should have plans both for good and bad turns in the economy. Adoption of sound management techniques and computer-related technologies is important.
Companies must remain Relevant with their processes; products and operate with Speed in today's Digital age.
Larger businesses should also have people that know how not just to manage the company but also its main asset, its people.

Cash and Only Cash can pay bills. The capacity of a business to pay its bills would stem from good cash-flow. A business could become cash strapped if it does not collect its accounts receivable on time. What is DSO? Isn't it a measure of ones capacity to pay? Say if a business has a DSO of 55 days. This means that at an average this business gets paid by its customers in 55 days. The question then arises that when will this business then pay its suppliers? In all probability the answer is that its capacity to pay its suppliers will be after 55 days. In this event you may want to evaluate its borrowing capacity to see if you can cajole this company to pay you in time even if it means that this business borrows to pay you.

This would bring on the analysis of how the debt of the company is structured in terms of secured and unsecured debt with an operating lender, generally the bank. Short term borrowing could be calculated as a percentage of the inventory and A/R on hand. One should look at the line of credit and see if there is capacity for more borrowing. Also check for any negative occurrences as bad checks (cheques) or any default against operating loans or covenants.

The capacity of your product to influence payment is also important. If your product being sold is fiercely competitive then it may not have the capacity to influence timely payment. If your product does not directly contribute to the COGS of the buyer then again it might not have the capacity of influencing timely payment. Competition definitely influences Capacity.

The Capacity to expose and increase your credit risk also depends upon your own ability and resilience to getting hit with either slow payment or perhaps no payment! Credit departments that have a lot of confidence in their collection ability and ability to influence payment have a wider capacity to expose and absorb. Your product-margin will also influence this capacity.

Capital:

Capital would refer to the financial resources obtained from financial records that a company may have in order to deal with its debt. Many a time's credit analysts would make this portion of the credit analysis the most important one. Weight is given on Balance Sheet items and components like Working Capital , Net Worth and Cash Flow.
One must know how to read financial statements and that too from the perspective of a creditor. Short term liquidity is important if you are expecting to get paid in the short term. You should be able to see whether this company has the ability to absorb more debt and then where does your loan (selling on credit is a loan - isn't it?) fit in the overall debt-framework of this business. You should also evaluate to see if you can depend on the numbers whether they are audited, unaudited or company prepared. If required speak with the firm or person who has

prepared the statements.
Leveraged borrowing depends on the equity/ net worth that a company has and it is a good idea to see if the company is committed to improve its borrowing-power by contributing to its

Equity/Capital/Net Worth . One way of doing this is by retaining all or portions of its earnings.
But all said, done and then undone Cash and ONLY Cash pays bills. Thus, keep an eye of the company's cash-flow and cash-position.

But one must be cognizant of the fact that financial records are snapshots of the past and credit analysis is trying to figure out the future. Thus all 4 Cs of credit are important in the overall analysis of a company or an individual where you combine elements of the past to make a futuristic prediction.

Conditions:

This refers to the external conditions surrounding the business that you are analyzing.

For example the construction industry might get influenced with the changes in the government's wide range of policies on immigration, interest rates and taxation.

There might be likelihood that a company that you are evaluating deals in international trade and a shift in the currency rates might have a detrimental or beneficial effect on it.
The events in the USA on Sept 11th have had added a new meaning to Force Majuere in context of International Trade terms and conditions. Air Travel has been impacted.

Ford recently announced closing 5 plants in North America asides from thousands of layoffs one will have to be vigilant on the impact that it will bear on the suppliers to the Ford Motor Company.

Business with local economies would be prone to the social climate and their influence on the local society. Torontonians must have heard of the flamboyant discount retailer "Honest" Ed Mirvish who treats the local community to free turkeys every Christmas. On another note a lot of businesses became insolvent in the Ice Storm a couple of years ago in eastern parts of the US and Canada that were totally dependant on

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the local economy. This winter) has been very mild and businesses that depend on snow are already feeling the crunch.

Again, one might look at how the internet is redefining business. Recently I was at a very small camera shop and soon realized that the business was generating big revenues on the internet and especially on e bay

All of this can again influence the ability or intention of a customer to pay his/her bills.

Thus in evaluating the degree of risk of a customer, information revolving around the 4Cs of credit would be normally necessary.

Assembling your jig saw –

To me Credit Risk Assessment is all about putting together all the relevant pieces of information you can get on a customer, it is like assembling a jig saw puzzle and the more pieces you get and the bigger the pieces are, the clearer the picture you will see and hopefully the better the decision you will make

Because Credit Risk Assessment is in a way an inexact science, you can only work on the basis of the information you have to hand. So you have to get as much relevant information as possible. This will be achieved by asking the right questions at the right time and knowing where to look and what sources you can rely upon and the ones you can't.

The first question is:

Is it worth granting credit?

In every business there is a lower limit where it simply doesn't make sense to give credit. There is the cost of processing an order, delivering the product, opening an account, sending out invoices and statements and the necessary collection activity that goes with it. The first thing you should do is to establish your figure. In some cases this figure might be €500 per month, maybe much less when you are selling high margin, low value goods. The figure could be significantly higher if you are selling high value low margin goods. The first task is to establish a lower limit and set your credit policy to say that anyone buying less than €X per month have to pay in advance, pay by credit card, pay cash on delivery, pay online – whatever you decide is workable for you. Be careful not to set this figure too high so it could have an impact on sales or too low so the profit you make on the sale and being more than swallowed up in administration charges. Remember the purpose of giving credit is to increase profitable sales, as a credit professional you have to look at both sides: the value of the sales and the profit being generated by those sales. The only possible exception to this rule is when you are in a start up situation and establishing a significant market share is the priority. Examples of this kind of business would be setting up a mobile phone network, you have high fixed costs and low variable costs, so the potential profit from each additional customer is high and the cost of adding them to the network is low. In that case minimal credit vetting would be the order of the day here and when you get to a particular size you can then become more selective about the type of customers you choose to do business with.

The next question is:

Is the amount significant?

On the basis you have limited time, and typically credit controllers, credit managers and risk analysts have more work to do than they have time available, so being able to effectively manage your time is a vital element in your success, the first thing you have to do is to establish what is a significant amount for your company. I have seen some small companies where €600 would be significant and I have seen some large multinationals where that figure is anything over €1m. In your business you have to establish what your figure is, and I hope you are getting at this stage that it isn't a fixed figure you work with regardless. The figure will change based on the business, the type of market you are operating in, your stage within the product lifecycle, what your competitors are doing, and your current marketing focus. So, as with most things in credit we have a few unbreakable laws and a number of flexible ones. In this case you should have a figure in mind and say for example anyone wishing to do less than €1k sales in a month will be subject to the minimum credit check.

What credit checking should we do?

As stated earlier the amount of checking you do depends on a number of factors the following is an extensive list of the information you can get, it is up to you to decide what is best for you right now. Before I go any further, you should have a written credit policy and you policy should establish different customer levels based on your industry. I suggest you have four levels – the figures below should be changed to suit your own business:

Level 1 – Below €500 per month – payment in advance is required.

Checking: We simply check the legal entity. In Ireland you can use the Companies Registraion Office, click here for the link . For Northern Ireland and the UK you can use the Companies House click here for the link.

Level 2 - €501 - €1,000

As per Level 1 – in addition:

- We will contact one of the trade references
- We will get an agency report or
- As a result of completing this course you can put their financial information into your scoring model to establish risk rating.
- Need a signed statement from the sales person that clearly states that they recommend the granting of credit to this customer. This can be a separate form or incorporated into your new account application form.
- Direct Debit is required.

Level 3 - €1,001 - €50,000

As per Level 2 – in addition:

- Contact two trade references
- We will get a full agency report with credit score and suggested limit
- Sales statement is signed off by Sales Manager
- Direct Debit is discretionary
- We will check the local business media for press reports in the past twelve months online.
- We will apply for credit insurance limits – if applicable

Level 4 – Over €50,000

As per Level 3 – In addition:

- Contact a third credit reference
- Sales statement is also signed off by the Financial Controller
- Personal visit to the customer's premises by the Credit Manager
- If they score less than X – up to date management accounts are required.
- If they score less than Y – a guarantee is required

Once you have established your levels you must make sure you complete the required checking. If the rules you initially set prove too onerous then revise the levels bearing in mind the resources at your disposal. When an account moves from one level to another the additional checks should be carried out. In the example above if a customer has a €1,000 line of credit in place and are looking for €2,000, then you should get a second reference, check them out online and get an agency report, and if you are happy sign off the new credit line.

You should create a check list for every new account application and every limit increase request – tick the boxes, make your decision and keep all the relevant information filed in the one place for future reference.

In all cases an application form is required.

You may decide to create rules for your customer visit e.g. If the limit sought is less than half the limit recommended by the agency you might decide a visit is not required and in some cases you may decide that a visit is only required when the limit sought exceeds the limit recommended.

When it comes to Agency reports it is important you have a provider you can trust. Different agencies have different scoring models and some have access to different information. At the core they all use publically available information such as CRO or Companies House, some of the larger agencies such as D&B, Experian, Stubbs Gazette and Creditsafe have access to payment performance data their clients share with them, which they in turn incorporate into their reports. If you are using a credit insurer they sometimes perform their own financial reviews and have more up to date information which should be relied upon more than simple reports.

The purpose of implementing a plan for new and existing accounts is to ensure the business is profitable and while other departments will have an input the final decision rests with the Credit Manager in all cases.

As soon as the account has been opened you should begin to rely on your own payment performance as a guide to the creditworthiness of your customer. If all payments are made on time they get a score, if some payments are late or there are some unpaid invoices at the end of the month, and as long as you are not the cause of these delays, they should get a different score. The highest risk of all is when the payments are getting later and later every month.

One other thing you have to take into account is your exposure to your customers, too many credit managers simply work on the month end debtors ledger for analysis purposes, and this can be a great mistake. You see, on the basis that your customers pay you at the end of every month, the balances you are looking at are typically the lowest the balances are going to be. If you are going to manage credit effectively you have to work on the maximum balance the account can get to.

Let me give you an example: You print off your aged debtors at the end of the month and Company A owes you €20k. They have made a payment on the last day of the month. If they are buying €20 k per month, you will supply them with another €20k worth of goods or services in the coming month, before you will get any more money from them. So your risk is not the €20k you are looking at but the €40k exposure the account will be at the day before you receive your next payment. We are not finished yet… If they pay you by cheque, your exposure at the end of the month is the value on the account plus the uncleared cheque, and cheques can take two or three days to clear. In addition you have to look at their buying patterns, do they order goods on a daily, weekly or monthly basis? In this example a company does €20k worth of business with you in the month, they pay by cheque on the last day of the month and to maximize their available credit they order the full months stock on the first day of the month, giving them up to 60 days credit, if payment is due on the last day of the month following invoice.

In this example your exposure is €60k – the €20k balance, the €20k uncleared cheque (that could bounce!) and the €20k order they received on the 1st of the month before the cheque has gone through. This obvious reality is missed by a number of less educated credit managers and can lead to real damage if not properly managed and controlled.

There are ways to reduce your exposure without limiting the amount of business you do with any customer:

- You can reduce their credit terms.
- You can ask for weekly payments.
- You can ask to have the money transferred directly to your account.
- For high risk customers you can ask for interim payments when the account gets to an agreed level.
- You can change your discount structure by giving annual rebates instead of giving discounts off invoices.

You should explore one or more of the above options when accounts are growing at a rate you are uncomfortable with.

With a proper risk plan in place combined with the financial understanding you will receive from this course you will be in a better position to see things that are going to happen long before they do and this will put you and your company in a stronger position.

Last point on assembling the jig saw – the more pieces you get the better, the bigger the pieces you get the better, the more you verify the information received the better. All this has to be completed in the shortest possible time, my recommendation is that most accounts are opened within hours of receipt of the completed documentation and you have access to the best online information and prioritise the function. If you find you and your staff are spending lots of time "releasing orders" that would signal a problem to me. You are better reviewing the lines of credit and revising them than simply releasing orders as long as they are within terms. If you adopt this policy you can soon find that balances can grow exponentially and when they get to a certain level it can be too late to do anything about it.

If you would like more information on this section or to see some sample reports, let me know and I will send them to you.

New Account Checklist

Level 1		Level 2		Level 3		Level 4	
Application Form		Application Form		Application Form		Application Form	
CRO Check		CRO Check		CRO Check		CRO Check	
		One Trade Reference		Two Trade References		Three Trade References	
		Agency Report		Agency Report		Agency Report	
		Sales Recommendation		Sales Management Approval		Sales Management Approval	
						Financial Controller Approval	
						Customer Visit	

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