Understanding the role of Credit in Business

Right from the start you need to know that credit is really more of a sales function than it is finance. We only give credit when it helps us to sell more. So giving credit is a sales tool we use to expand our business. In Credit, we spend our days dealing with customers, we have clear goals, we make calls, we keep accurate records, we overcome objections, we hit targets and we get result. If you read that last sentence again – could that job description be for anyone else? Could it be what you would expect a sales person to do?

The success of every business depends on Sales and Credit working together in harmony to serve the customers to generate the required level of sales and then to collect the money due in full and on time. You see the purpose of any business is to make money and the job of the collector is to bring that money into the business.

The reality is that most Credit functions report into the Financial Controller or Finance Director and while I see why that is, it is often an uneasy fit because the dynamic nature of credit does not fit very well into the more black and white world of accounting. We have financial responsibility and the focus of Finance is on the money and as we are the ones charged with the responsibility we usually form part of the finance team.

There is a lot more to credit than just collections. Credit is about selecting the correct customers, setting appropriate terms and lines of credit for each customer, administering the account in a professional manner, generating the correct reports and it is about getting the money and keeping the customer current and buying.

This course is going to focus just on the collections area. If you enjoy the content, if you find it really useful in your day to day job. If you can implement some of the strategies on a daily basis to get better results from a cash perspective you might be tempted to continue your studies and go on to learn all about the other aspects that will ensure even greater success that is for another day.

We hear a lot about banks not giving credit and in a study by the Kelley School of Business for the Central bank of Ireland they found that Companies who were constrained in their borrowing capacity by the banks, used trade credit as a source of funding for their business, hardly surprising that due to banking constraints customers tend to delay payments to their suppliers.

Credit is the lubricant of business. The effective management of Credit keeps the wheels of commerce turning. Up to 90% of business to business transactions are on some form of credit basis so you would think it is in the businesses interest to take the function seriously and to make sure collectors have all the resources they need to do their job efficiently and effectively.

A key part of the role of a Trade collector is to keep accurate records. There are two main areas of concern; firstly accurate records on the customers and the six items listed above and secondly, accurate records on every call that was made, who made the call, who they spoke to, what time the call was made, the duration of the call, what was agreed and what date a follow up action is required if the promise has not been acted upon.

You must always treat your customers with respect and dignity. Sometimes collectors see the people they are talking to as just an endless stream of debtors, debtors who are in default and need to be shown the error of their ways. If you adopt this approach you will have a day filled with hassle and arguments. You need to view each call as a unique individual and be able to adjust your collection style to match the communications style of the person you are talking to. This area will be discussed at length in Module 4.

The role of collector also includes knowing what information is available and where to get it and what to do with it when you have it. The first source of information should be your Credit Application Form. This should be completed for every credit account that is opened. If you haven’t got a formal account opening process or you have only recently acquired one, it is a good idea to get all existing customers to complete an application form at some stage and this can be done on a phased basis based on the risk category of the customer.

I have shown below a copy of a suggested Credit Application form for Business to Business purposes, I am sure there are elements that could be incorporated into your own form to improve it.

Insert

Your Logo

Here

Insert your Companies Name, Address, Accounts Phone Number, eMail address, website

Fax No

New Customer Information

Trading Name ____

Legal Name____

Trading Address____

Delivery Address____

Tel No_________ Fax No: ____________ Mobile ________Website www.________

Business Type:

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

Registered Number____

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: ____________________

Initial Estimate of monthly purchases €____________________________________

Type of Business ____

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 ☐

For office Use only:

CRC ☐ CC ☐

DT ☐ SPC ☐

VN ☐ CAN ☐

CLA ☐ CRC ☐

PB ☐

AB ☐

Other (Please specify) ☐

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

5 Banks may refuse to accept instructions to pay direct debits from some types of account

6 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 ___________________________________

It is not the intention of this course to go into detail on the component parts of this form that is reserved for the Credit Management course -this course will focus on just collections, so from your perspective you should have easy access to these details to help you in your collection role.

The importance of your Customers

"The purpose of a business is to get and keep a customer" this quote is attributed to Legendary Harvard Business School Professor Theodore Levitt and is an adaptation of management guru Peter Druker who said "The purpose of a business is to create a customer". Without customers you don't have a business, so it is vital that every customer is looked after and treated with respect.

Because of your role and you are the only person in your organization who is looking for anything **from** the customer (everyone else is looking to give something **to** your customer) there can be some level of conflict. Rule number one is "never fight with your customers" – there can only be one loser.

Your customers are the reason you exist as a business and they are the reason everyone does what they do.

The job of collecting money from other businesses is an important and often underrated one.

Credit Controllers and Collectors spend more time each day talking to customers than the sales people do. In my experience they also care more about the customers than the salespeople do. Most of the time spent resolving queries and disputes are solving problems that are being experienced by the customer. Most of the internal issues where your company has let a customer down in some respect and it is the job of the credit team to put it right in the shortest possible time. How you deal with a customer has a dramatic effect on the overall business, with proper systems, procedures and the correct attitude the credit team are a valuable asset to the business. Get any of these elements wrong and the credit function has the power to destroy a business.

Understanding Credit Terms and Credit Limits

In simple language your Credit Terms are the amount of *time* you are prepared to offer a customer to pay their account and Credit Limits (I prefer the words Line of Credit & I'll explain why later on) represents the *value* of credit you are prepared to extend to a customer.

The great thing about Credit Terms is that you get to decide what you give to whom. There is a misguided notion out there that if you are in business you have to give credit, I'm here to tell you, you don't.

Since August 2002 businesses have been entitled to charge interest on Late Payments on all Business to Business transactions. My experience is that most still don't. In some cases this is a waster opportunity. I can see why some business owners might be afraid of the damage it could cause to the relationship by charging interest. In some cases when the account is many months old, the relationship has already broken down, and the point of breakdown is the point when you would no longer accept an order from them. In this case why not charge interest? If you are handing an account to a collection agency, the relationship is gone, add the interest charge before you send it for collection.

What should your terms & conditions contain?

Every business must have clear terms & conditions to set out exactly how they do business and their own rules around supplying goods & services. Clarity and simplicity are the keys here and rather get into a load of legal jargon; I have compiled a number of questions that need to be answered, to be incorporated into your own terms, if relevant.

This will make sure your relationship with your customer remains healthy and free of conflict.

If doing business on an ongoing basis you have to be clear regarding when the contract is made and with whom. You have to state when the title to the goods transfers to the customer, does title transfer on order, on delivery, on payment or when all invoices have been paid in full? Do you have the authority to enter their premises to get your goods?

What about quotations, how long are they valid for? Are they binding?

Is the contract assignable?

If one provision of the terms is invalid or unenforceable does that negate the rest of the contract?

What about delivery, when and how soon will goods be dispatched following the receipt of order? Will you ship part shipments? How long does the customer have to report shortages and damages?

What about pricing? What determines the price point? Is the price driven by order date, delivery date or invoice date? Are prices subject to VAT?

What about payment? When exactly is payment due? Is it 30 days from date of delivery, date of invoice or end of month following invoice? Is there an interest charge? Is there discount for early settlement?

What about circumstances outside your control?

Who is liable?

In what jurisdiction is the contract made?

Do you offer guarantees?

What happens if the decide to return stock to you?

Last point, always get legal advice in compiling your published terms & conditions, make sure they will serve you. You must communicate your Terms & Conditions to your customers at the earliest possible time. It is not good enough to print them on the back of your invoices. An invoice is a post contractual document and will not stand up if it is the only notification. Never lift terms & conditions from another customer or supplier – by all means use them as a guide and adapt them for your specific business. Most importantly if you do nothing else having read this article, please take the ten minutes to read and understand your own published terms and conditions, there will be at least one thing in there that will surprise you, and it will also increase your own confidence when you are able to quote your own Terms and Conditions if required. There is nothing worse than sounding unsure on the phone or in person, it immediately puts the other person in a position of power.

The question I asked in the original material is "Do you have clear credit terms that are communicated to everyone internally and externally and are strictly adhered to?"

There are many dimensions to that question:

When I say "clear credit terms" I mean it. Is the reader completely clear exactly when payment is expected and when it should be made? Too often I see lines like "30 days" or even "Nett 30 days" or "Net 30 days" or "strictly 30 days" and to be honest if you ask ten different people you will probably get ten different answers. If goods are ordered today, dispatched tomorrow, delivered the day after, invoiced the day after that and the invoice is received by the buyer next Monday what date should payment be made?

Is it 30 days from date of order, date of dispatch, date of receipt, date of invoice, date of receipt of invoice or even month end following invoice?

What do you mean when you say payment? Does that mean the money is in your bank? The money has been sent from their bank? The cheque is on your desk? A bank draft is on your desk?

The great thing is that if we can have so many different answers from the credit people – just imagine how many variations you will get when you add your sales people, your customer's buyers and their accounts payable departments and finance people.

As the person responsible for credit, it is your job to explain to all relevant people exactly what you mean through examples:

Payment is due on the 30th day following the date of invoice
Payment is due on the 28th day of the month following invoice
Payment should be in our bank on or before ______________

If you are looking to be paid on individual invoice – this works best if you have a one off purchase – if you are supplying goods on a daily, weekly basis do you really expect to get a cheque every day 30 days after the date of each invoice – leading to many cheques being issued and received increasing the workload on both sides – may not be considered a great idea.

One line I hear often that upsets me: "Oh, our terms are 30 days but nobody takes them seriously"

It is up to you to take them seriously, it is up to you to make sure everybody knows exactly when payment is expected, and it is up to you to make sure payment is made exactly when it is expected.

One of the first things we do when we provide an independent credit health check to our clients is to make sure they are sending out a consistent message, from their New Account Application Form, Their Terms & Conditions, Their Invoices and Their Statements – you would be amazed how many times there are inconsistencies here.

I always maintain that Credit Management is simple, it is up to you to keep it as simple as you can and this is a very important area that will decide how successful you will be in the Management of your own Credit.

This is the first important step to achieve success in Credit.

Dealing with Sales and other Departments

In some businesses there is conflict between sales and credit. Sales often have a negative view of the credit function; I have heard the credit team described as the “sales prevention department” or the “anti sales squad”. The only contact coming from the Credit department tends to be negative. The discussions are around overdue accounts, accounts on stop supply or other queries and problems. As a Qualified Collector you have to find ways to reverse this trend and become more positive in your communications.

If there is a customer query or dispute, your motivation has to be to keep the customer happy by resolving the issues on a timely basis and as long as you are interacting with sales with a view to keep their customers happy they will respond in a more positive way.

The debate has been raging for many years now as to where the credit function best fits within an organization.

Is credit a finance function reporting to the Head of Finance?

Is credit a sales function reporting to the head of sales?

Is credit a standalone function that exists somewhere between the two?

Where ever the function fits in your organization depends on how you view the function and your definition of what a sale is.

If your sales people are target driven and they are rewarded for bringing orders into the business and their involvement ends there, then it is best to have credit as part of your Finance team overseeing the process.

If your sales people are rewarded on the basis of cash received then it is best to share the credit expertise with the sales staff, and if you count the sale when the money goes into the bank then you are better off having credit as part of sales.

If you have a large business where the professional management of credit is vital, you might be better off having it as a standalone function reporting to a Director of Credit who is responsible for managing the margin from start to finish.

Whatever way you structure it, you can be sure of two things: there will always be some level of conflict and every member of your staff has to work together for the benefit of the whole business.

It is important to look at what results you will achieve by the different approaches before you decide what is best for you. If you reward salespeople for bringing in orders, they will be more likely to bring in higher risk accounts, they are more likely to be annoyed if an order is held for any reason, and they are more likely to demote the collection of money to the lowest priority on their daily task list. At the end of the day if they can only make one more call and the choice is between making a sale or collecting a cheque, they will make the sale every time.

If you reward salespeople on the basis of cash received they will end up spending a large proportion of their time collecting money from customers, they are more likely to qualify their buyers and at the end of the day if they can only make one call and the choice is between making a sale or collecting a cheque, they will collect the cheque every time.

It might come as a shock for you to hear that my views are not what you might expect from the Credit Coach, I believe salespeople should sell and credit people should arrange the payments. Credit and Sales have to work together and in an ideal world I would like to see a system as follows:

The sales person brings their prospect list to the credit controller or manager – the list is vetted and the salesperson told in advance the ones they should concentrate on and the ones that will not be offered credit by the company.

The sales person clearly agrees payment terms with the customer in simple terms, if it is a monthly account they should explain that you will supply goods for the month of June and you expect to be paid on the 28th July for them.

The sales person clearly agrees pricing and details of the service that was promised and takes responsibility to communicate that to the relevant person in the office.

If the salesperson works to a journey plan, that should be communicated to the credit controller who can say to the customer: “John will be in Castlebar next Tuesday will you have a cheque for €x for him?” When the commitment is received the request is passed on to the salesperson who collects the cheque as agreed.

The salesperson is kept informed on the status of all their accounts and should get notice if there is a chance that credit will be withheld from any of their customers at a future time.

Time should be set aside every week/ month for the credit controller and salesperson to discuss the contacts with the customers, the issues they are having, with a view to resolving customer queries in the shortest possible time.

Working together for the benefit of the whole company is the key to success.

This is the end of module 1 – I hope you enjoyed the content. Please complete your short test if you haven’t already and submit it to me for marking. You will receive Module 2 on two weeks’ time.