

Credit and Debt Collection

You may have a few loyal customers or companies who make large orders and purchases. Should you issue them credit, and if so, how and when do you collect?

By **Abe WalkingBear Sanchez**

You'd think the goal for the credit and collection department is to find ways to reject new customers and drive away old ones, based on the use by most of their representatives of traditional DSO (days sales outstanding) and bad debt performance measurements.

Retailers extending credit terms often have more money tied up in accounts receivable than any other asset. Next to cash on hand, accounts receivable is the most liquid asset available, being but one step removed from money in the bank. Yet, the credit and collection function, which is responsible for creating and managing accounts receivable, may be the most misunderstood, underutilized and undervalued area of business.

WHY AND WHEN

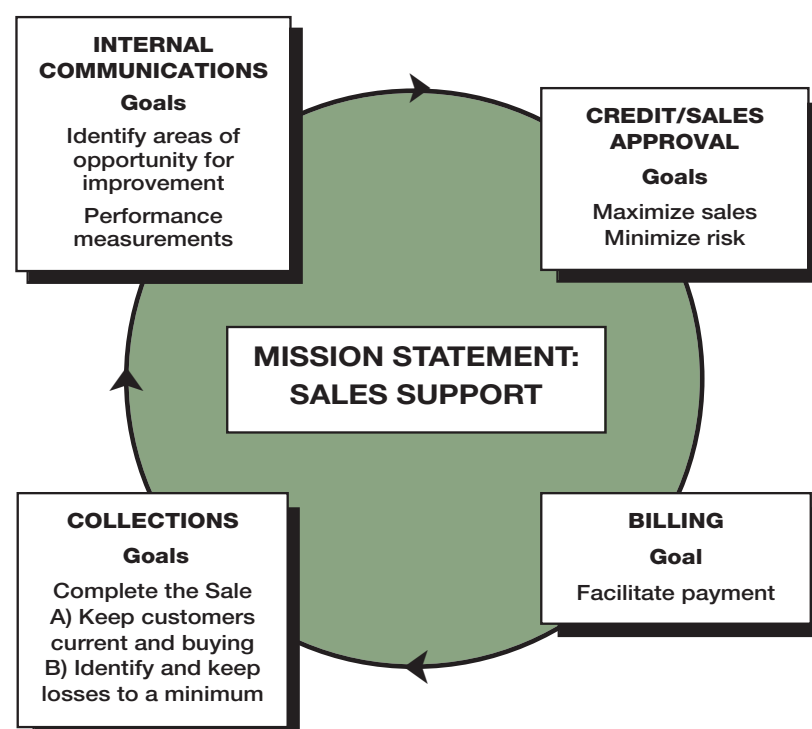
Extending credit creates costs and risk. There's the cost of gathering information on new cus-

tomers, obtaining reports and ratings and evaluating the customer and the sale. If approved, there's the cost of setting up the account and of billing/accounting. Further, if a company borrows on its accounts receivable, there's additional debt service cost. Should the customers not pay when due, there's the cost of holding the debt, collecting on it and possibly writing off bad debt.

If extending credit creates costs and risks, why not dump credit, go to a cash and carry system and pass the cost/risk savings on to customers?

Simple: There are customers who require that vendors/suppliers provide their product/service and then give them time to determine if they received what was ordered and to process the bill for payment. There are customers who must sell to their down-line customers and collect from them before they can pay their own creditors. And there are competitors who offer credit terms. ♦

Figure 1. Each component of the credit process must be propelled by a goal(s) that remain true to the Sales Support mission statement.



Above: Landscaping services often require credit. Do you know how to collect?

The only reason anyone should extend credit to customers is in order to get a sale that would otherwise be lost. If your customers can and are willing to pay at the time of purchase, don't force credit on them, just grab the money.

MISSION STATEMENT

Credit is the selling of a product or service based on payment at a later date. It is the lubricant of commerce that allows for the expanded movement of products and services. It is a sales support function.

Yes, there's risk associated with extending credit, but risk avoidance must not be the primary focus. Sales Support is why credit exists, and that must be the vision that drives the credit and collection area of business.

Credit approval, billing, collections and internal communications (performance measurements and reports) are the major components involved within the credit function. Each component must be propelled by a goal(s) that remains true to the sales support mission statement (see Figure 1, page 48).

MESSAGE

Wrong Message. The credit approval process has at times been described as finding ways to say no, and the credit department has been referred to as the sales avoidance department. Considering that the credit people are being told, via performance measurements, that risk avoidance is the goal; it's surprising that any customer gets approved.

Right Message. The goal of the credit approval process should be to maximize sales and minimize risks. Working to find ways of saying yes to every possible sale while remaining confident of payment better complies with the sales support mission statement.

Credit customers are funny. If you don't send them a bill or send one that is late, incomplete, has errors or isn't understandable; they won't send you money. The goal of billing is straightforward and simple: facilitate payment.

While delinquent customers can make up 25 percent or more of the total accounts receivable, less than 1 percent (on average) are ever written off as a loss. Most past dues are good customers who will pay; there are reasons why they pay late. Contrary to the old enforcement of payment mindset, collections is the process of completing the sale. The goals are 1) keep customers current so they buy from you, not your competitor and 2) the early identification and control of potential losses.

Don Rice, of Texas A & M says, "Employees respect what management inspects not what management expects." How you track the ongoing processes and the measurements you employ are essential to achieving desired results. Tracking the credit approval phase by the time it takes and the effort exerted to find a way to make the sale, re-enforces the maximize sales/minimize risks goal. Billing should be measured and tracked to ensure that it's timely, accurate, complete and understandable — that it facilitates payment not hinders it. Collections must be gauged and measured by current customers and the early identification of potential losses. The goal of reports and performance measurements must be to bolster the sales support mission statement, not contradict it. ♦



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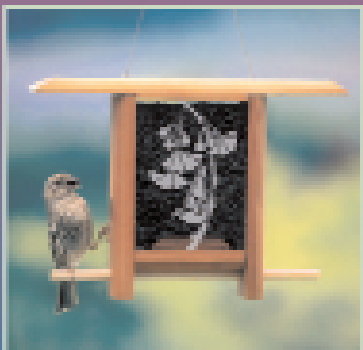
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MANAGEMENT



Do you collect payment at delivery? Maybe credit will work better in this instance.

PROCESS AND PEOPLE REQUIREMENTS

The step-by-step processes must be driven by the goals and lead to their achievement. Question why things are being done, and the how will follow.

All too often the wrong people are involved in credit and collections. People do best with the things they like to do. Evaluate your present staff; are they communicators? Do they enjoy customer contact and problem solving? Are they organized and detail oriented, and do they have good follow-up skills? If not, you have a problem.

THE CUSTOMER/SALES SUPPORT DEPARTMENT

"Two men look through the same bars; one sees the mud the other the stars."

The credit and collection area has long been seen as a negative, a cost center and a necessary evil. In order to change this belief a new vision is required; one that is more in keeping with the reason why credit exists. Changing the old credit and collection department to the new customer/sales support department reflects the new vision of credit as being a positive and a profit center. Remember, expectations will wither without proper guides, processes and monitoring. ☞

BENEFITS

What can you expect from a sales- and profit-driven credit and collection function?

- An expanded customer base
- More sales
- Better customer service
- Speedier turntime on accounts receivable
- Controlled bad debt losses
- Improved efficiency
- Higher staff and customer retention.

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