Covering Credit Bulletin

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Alternative Dispute Resolution - Pro's and Con's

Alternative Dispute Resolution

Some creditors include Alternative Dispute Resolution clauses in their contracts, credit applications and invoice terms. Alternative Dispute Resolution involves the use of specific tools for resolving disputes between buyers and sellers. There are advantages and disadvantages of Alternative Dispute Resolution including these:

Pro's

- It is not necessary that each side be represented by an attorney
- ADR is a private and confidential process, not subject to public scrutiny or to public disclosure
- There is no jury, and therefore no possibility of swaying the jury with emotion or sentiment
- ADR costs less than litigation
- ADR takes less time before the matter is heard
- · Hearing are typically far shorter than trials
- With ADR, there is always the possibility of resolving the dispute without destroying the business relationship

- Binding arbitration results in a decision that can be enforced in Court if necessary
- ADR is a private and confidential process, not subject to public scrutiny or to public disclosure
- An arbitrator or mediator can be selected who has specific knowledge in a particular field or industry. That individual can apply his or her knowledge to the testimony and the facts presented.

Con's

- It is not necessary that each side be represented by an attorney
- ADR is a private and confidential process, not subject to public scrutiny or to public disclosure
- There is no jury, and therefore no possibility of swaying the jury with emotion or sentiment
- With binding arbitration, the loser has limited remedies if the decision goes against them and against the facts
- The arbitrator has no power to enforce the decision or judgment
- If arbitration is non binding, neither party is required to accept the decision of the arbitrator
- Discovery is often limited and arbitrators or mediators do not have subpoena power
- An arbitrator or mediator can be selected who has specific knowledge in a particular field or industry. This means the mediator or arbitrator may bring along his or her personal prejudices and biases

ADR is an informal dispute resolution process. ADR includes arbitration [both binding and non-binding] as well as mediation. Before deciding about whether ADR is right for your company, it would be a good idea to discuss it with senior management and with your employer's attorney.

Questions and Answers

Question: What are your thoughts about giving performance bonuses to collectors? I have been approached by my collectors following a credit group meeting that one attended in which bonuses was one of the topics discussed over lunch.

Answer: I am in favor of any arrangement that benefits both the employee and the employer. In my experience, the key is to develop a system that rewards the right kind of behavior. For example, it would be inappropriate to reward collectors based on the quantity of outbound collection calls made unless the bonus also took

into account the quality of the work done during those calls. It would also be wrong to bonus a collector who uses inappropriate tactics to collect money such as threatening to place every customer they speak with on credit hold unless they receive an immediate commitment for payment of the past due balance.

- Q. I received an unsolicited offer from a company to buy my claim in a bankruptcy for 25 cents on the dollar. Why would they make this offer?
- A. Companies that buy debt do so because they believe they will receive much more than they paid you when the case is settled.
- Q. Any comments on formula driven credit limits?
- A. I have a few general comments. The first is that credit decisions should be customized; there is no one right way to establish credit limits. I have used and find value in sophisticated credit scoring models that perform sophisticated multivariable analysis in recommending a credit limit. I would be concerned about using less robust software, and I would avoid a simplistic approach to establishing credit limits such as this "10 percent of the applicant's audited net worth or 5 percent of the applicant's unaudited net worth."
- Q. I just reviewed my employer's credit report. There were numerous errors. Who should correct these mistakes, and how is this done?
- A. Ask your manager if she or he wants you to take care of it. I would mark up a copy of the report and forward it to the credit reporting agency. I recommend you do this through your salesperson and tell them you want them to send you a corrected copy within thirty days.

Congratulations on taking the time to review your report. Many companies do not review their own reports. I recommend that clients do so at least once a year. That way, creditors and other interested parties have access to current information.

- Q. My sales department has asked for a \$20,000 credit limit for a new customer. What credit limit would you assign [any why] to <u>Customer Name</u> based on the attached credit report?
- A. Sorry, I will not answer this question. Hypothetically, before I answered the question, I would need to know more about your company including: Its profit margin, loss history, size of its bad debt reserve, management's tolerance for delinquencies, and more generally its tolerance for credit risk. However, I do not offer opinions in this public forum about any company's creditworthiness. There

are legal risks associated with doing so, and the Disclaimer I would need to add would be longer than the answer.
Website of the Month
Here is the website of the month. SEDAR is the Canadian version of the U.S. EDGAR Archives. It contains financial reports and other documents filed by publicly traded companies across Canada. Access to the information is free and the URL for this website is: http://www.sedar.com
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Webinar Schedule

"Handling a Distressed Debtor." This program will be offered on June 8, 2006.

"Antitrust Issues Facing the Credit Department" is offered on June 15, 2006.

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