Covering Credit Bulletin

June 2008

This Month's Topics:

- **Personal Responsibility**
- **Questions and Answers**
- **When Mistakes Happen**

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Personal Responsibility

Members of the credit department should take personal responsibility for the credit decisions made by the department, even if they played only a small role in the decision-making process. In a scenario in which the final credit decision was made at a higher level, the person notifying the customer should take personal responsibility.

The advantage of accepting personal responsibility for the decision irrespective of who made is that doing so reinforces the idea that the person speaking to the customer is a part of the decision-making team and a part of the decision making process, rather than a clerk or a messenger. If members of the credit department want the respect of the sales department and of customers, they cannot pass the buck any time a difficult or controversial decision is made.

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Questions and Answers

Question: In response to collection calls, one of the most commonly heard requests is a request by customer to forward a copy of the outstanding invoice or invoices. What is the best way to handle this request?

Answer: Often, a delinquent customer will use a request for invoice copies as a way to delay payment. The collection staff should ask a number of questions each time a customer asks for invoice copies, including these:

- **To what address it is attention should our invoices normally be mailed?**
- **Has this address changed recently?**
- **To whose attention, and at what fax number should these invoice copies be sent?**
- **According to our records, this invoice corresponds to your purchase order number xxx. Is this purchase order number open and valid in your system?**
- **Do you have record of receiving the product referenced by the purchase order associated with this invoice?**
- **Is the only reason this invoice remains unpaid that you do not have an invoice copy?**

- **Once you have received the invoice company, is there any reason that the invoice(s) cannot be processed in paid this week?**

Q. I heard recently that in California a credit application signed by a customer will not be binding on a Corporation unless it is signed by two officers. Comments?

A. This is actually a fairly common question. This is a good question to ask your attorney, and I would encourage you to do so. As I understand the law, a creditor party may not know whether the people claiming to act on behalf of the corporation have been authorized by the corporation to enter into a particular transaction. Unless you know that a corporate representatives do not have authority from the corporation to sign the document, the contract will be binding on the corporation if it is signed by two corporate officers with one officer having general operational responsibilities such as the Chairman of the Board, President, or any Vice President, and one officer having record-keeping or financial responsibilities such as the Secretary, Assistant Secretary, Chief Financial Officer, or Treasurer.

To me, the tough question involves whether or not it makes sense to start pushing back credit applications from corporations and requiring signatures from two officers each time. I am thinking in particular about how difficult it would be to get such a signature from the two officers of a Fortune 500 company --- recognizing that it is sometimes difficult to get customers purchasing agents to complete and sign a credit application. To complicate matters, many creditor companies headquartered in California do business across the country. This question and these comments only address the signature authority of California corporations. Other states may have entirely different rules and laws.

If anyone has any comments or additional questions, I would enjoy hearing from you.

Q. I have a related question. One of our customers returned our credit application with certain language crossed out and initialed. What effect does this have on the terms? At no point did we indicate that these terms were negotiable. We certainly do not want to agree to the changes proposed. For example, the customer has indicated that they will not be paying are collection costs in the event that you must place the account with a third party for collection, the customer would be responsible for that this customer on delinquent balances.

A. Actually, this is a great question and another good one to discuss your attorney. The credit agreement that you ask the customer to sign is a contract. The fact that they have changed the terms of the contract represents a counter-offer. It is my understanding that if you do nothing, you will in effect have accepted the changes proposed by the customer in their counter-offer. Since it seems that you do not want to allow the customer to make these unilateral changes, you should contact the customer and explain that these terms are not negotiable, and that the account cannot be opened until a new credit application is signed by the applicant acknowledging that your terms and conditions of sale will control the relationship between you as the seller and the applicant has the buyer.

One additional note of caution: Often, the terms and conditions which appear on credit applications are inadequate to provide the necessary protection for the creditor company. In my opinion, it is essential that the credit application contains all the necessary terms and conditions to protect your company in the event the customer claims that your products or services caused some form of financial harm. I believe it is essential to ask your attorney to review the terms and conditions listed on the credit application to ensure that they provide all of the necessary safeguards.

Q: One of our customers informed us that their bank had seized the assets of the company, and they were in effect out of business. What are our options?

A: I would encourage you to consider asking these questions:

- **Does your company have a reclamation rights for shipments made shortly before the seizure?**
- **Under what legal theory or authority to the creditor seized the debtor company's assets?**
- **Was this company a secured creditor, and what form of security did the creditor hold?**
- **As a result of this seizure, has the debtor company filed for bankruptcy protection? If not, are they planning to do so? If so, when?**
- **Does your company hold any security or collateral, and what steps you need to take to preserve your rights?**
- **Would you put the explanation you have provided to me in writing?**
- **Have you notified other creditors?**
- **What is the name of the bank, and what is the name and telephone number of your primary contact?**

Q. I was hired a few months ago as their credit manager. In response to the CFO's request for an update on the deduction problem, I responded some of the deductions were as much as four years old and that (1) based on the age of these deductions and (b) based on the fact that they have not been actively worked for at least a year and (c) because these deductions were taken by some of our largest customers, that in my opinion it is unlikely that we will be able to collect more than 25 percent of the balance due. The CFO told me that it was imperative that I find a way to address and resolve these problems since the annual audit was scheduled for in July. How would you address this problem?

A. Essentially, you're being asked to convince your company's best customers to repay deductions as much is four years old. In my opinion, this simply is not can happen. Many of the larger retail customers are now notifying vendors that disputes and deductions that are not addressed in detail and in writing within 90 days of the date of the deduction will be considered by the customer to be legitimate and closed.

I suggest that you ask your CFO for permission to schedule face-to-face meetings with your larger customers. Before that meeting, supply these customers with all necessary supporting documentation relating to the outstanding deductions that you want to address and resolve. In occurs to me that your CFO is not interested in your opinion about the

collectibility of outstanding deductions, and he or she is unlikely to be convinced by anything short of a flat *NO* from your largest customers in response to a direct, formal and specific request that open deductions be repaid promptly. I think the chances of resolving this problem are remote, and even more remote if you do not try face-to-face meetings.

Q. One of our customers has over $5,200 over 90 days past due. They have ignored multiple messages, in addition to disregarding several letters and fax messages about this past due balance. As a result of their failure to pay and their refusal to respond, this account has been on credit hold for more than a month. There is an order pending for $6,000. The company's owner just called me and made this proposal: "I will pay the $5,200 by the end of the week if you release immediately the order pending for $6,000." How would you respond?

A. It is unlikely that I would respond by releasing the order pending. I suggest a counter-offer. Ask that the customer first pay the entire past due balance by wire transfer – at which point you will update the credit file and give serious consideration to reestablishing open account terms.

Q. Would you rather hire a highly motivated new credit and collection representative, or a highly skilled individual?

A. I would prefer to hire the highly motivated individual based on this premise: I can train a motivated and willing individual to be effective in this position, but I cannot train anyone to be motivated and diligent in their work.

Q. My manager has developed this basic rule for the credit department: There should be no more than three orders on credit hold at any time. Do you think this is appropriate?

A. I do not. I would encourage you to speak with your manager about the fact that credit holds will be necessary and appropriate from time to time, and that there is nothing *magical* about having three or less orders on credit hold at any given time….either the decision to hold is appropriate or inappropriate.

Q. Would you agree to sign a confidentiality agreement in order to get financial statements from a privately held customer?

A. I have done so numerous times. Privately held companies often have a policy of not providing financial information to unsecured creditors but will make exceptions if that creditor will sign a nondisclosure agreement. My one caution would be to make certain that your company is willing and able to honor the terms of the confidentiality or nondisclosure agreement, and once again this may require the assistance of your attorney. I would ask your attorney two questions. First would be whether or not to sign this particular nondisclosure agreement. The second would be whether it is appropriate and permissible to sign any nondisclosure agreement presented without your attorney's review and approval.

Q. A salesperson has offered to personally guarantee the debt of a new customer. Do you have a problem with this?

A. I would suggest that you accept a guarantee with these four conditions in place: First, the salesperson must be willing to sign a personal guaranty agreement – a legally binding contract. Second, the salesperson must agree that the guaranty will become enforceable if any portion of the account becomes more than 90 days past due. Third, the salesperson must be qualified for the credit limit for which he or she is to become personally liable… otherwise the personal guaranty would in effect be valueless. Fourth, agree to this arrangement if and only if it is first approved by senior management.

Please remember that you would be setting a precedent by accepting a personal guarantee of the salesperson. Personal guarantees are enforceable in a court of law. This implies the need to sue the salesperson if he or she refuses to pay voluntarily in the event the debtor defaults. It is important to remember that employers usually do not have the right to deduct money directly from an employee's wages except for required deductions such as taxes, or voluntary deductions such as those covering 401(k) contributions… meaning that you cannot do automatic payroll withholdings or deductions to recover money that you consider to be owed under a signed personal guaranty. You may or may not be able to do so if the debtor defaults and the salesperson/guarantor signs a Promissory Note relating to the unpaid balance and specifically indicates that he or she wishes to have a certain amount taken out of each of their subsequent paychecks to retire this outstanding balance.

One note of caution: labor laws are complex and very someone from state to state. This of course is another question for your attorney or CPA.

Q. I learned recently that one of our largest competitors has a UCC-1 security interest in the assets of a customer that is not currently even on our watch list. I have updated the credit report and can find no indication of deterioration in this customer's financial performance that would suggest or indicate that we need additional security or collateral in order to continue to extend credit to this company. What would you do in this situation?

A. I would give serious consideration to the idea of requiring the customer to provide a security agreement if I thought that the customer presented a serious risk. Unfortunately, I do not have enough information about the customer to comment about whether or not it is appropriate to continue to extend open account terms without any additional assurance of payment. Perhaps an appropriate intermediate step would be to request that the customer provide you with a copy of their financial statements rather than relying on the information contained in the credit report which may be out of date.

Q: I read that you recently lost your job due to a layoff. What advice would you offer to other credit professionals concerned about the possibility of being laid off?

A: Downsizing is a permanent feature of the American business landscape. Downsizing is almost inevitable in many industries for companies under pressure to minimize costs and increase profits. Credit professionals can no longer take job security for granted and

should proactively address this risk or threats - as they do any other threat they are made aware of - meaning they should attempt to manage and minimize this risk. Consider the following basic guidelines:

- **Keep your resume current**
- **Make sure your resume highlights your accomplishments and abilities, rather than having a resume simply provide a chronological history of you work experience**
- **If you are not actively networking with other professionals, start doing so. Start with executives in your local NACM affiliate, your industry credit group, your alumni association, or any other groups or organizations you belong to**
- **Investing in yourself through continuing professional education. Doing so can create a solid foundation for a job transition**
- **Seek out new challenges on the job. For example volunteer for a leadership role in working groups or task forces being organized by your company. You want management to view your contributions as more than one-dimensional.**

Q. People do not seem to know how to write emails. Any suggestions?

A. When composing e-mail, I suggest the following rule should apply:

- **Senders should spell check and proofread e-mails for errors. Remember that the spell check function will not catch everything**
- **Use complete sentences and appropriate punctuation**
- **Make certain that the message line is meaningful to the recipient**
- **Be brief --- or in the alternative offer a short summary if you are sending a long message**
- **Indicate the specific action you expect the recipient to take, and the time frame in which that action should be taken**
- **End your e-mails with a thank you**
- **Include any appropriate supporting documentation as an attachment to the e-mail message**
- **Make certain that the e-mail is professional in every way**
- **Remember that an e-mail is a permanent record, therefore make certain that you don't write anything that you be embarrassed about later**
- **Try not to write e-mails in haste or in anger**

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<u>Mistakes Happen</u>

The typical credit professional makes dozens of decisions a day ranging from whether or not to release orders pending, to which customers to call and in what order. These decisions must often be made in a high pressure, fast-paced business environment. Occasionally, decisions must be made with limited information. As a result of all of these factors, mistakes are sometimes made. When you make a mistake, you must:

- **Try to learn from your mistakes. Most of us have heard the old adage that failing to learn lessons from mistakes means that the same mistake is likely to be made again**

- **Do everything you can to avoid making the same mistake twice. Employers are often willing to overlook or make allowances for one honest mistake, but are less accepting or forgiving of repeated errors of the same type**
- **Although it is easier said than done, try not to waste time worrying about mistakes. Instead, spend time trying to reduce the impact of the mistake you have made**

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About the Author

Michael Dennis is interested in consulting and contract work, temp to hire work, or a permanent employment opportunity. His e-mail address is: mcdennis13@yahoo.com