Credit Management Squares the Circle

Customer focus and credit management – just five words, four of them significant standing alone, but of paramount importance when taken together to make up the five. They should be taken together, because as important as they may be, each in its own right, not to recognise the value, significance and impact of the whole misses the point entirely.

Customer

All customers are important – it is easy to recognise that some are more valuable than others in terms of the business they do with you. The well known and universally accepted Pareto principle clearly shows that in general, some 20% of customers account for 80% of business. It follows that this 20% require special attention when it comes to collections and contribution to cash flow, but that does not mean that the remaining 80% of customers who only account for 20% of business are unimportant. On the contrary, *all* customers have the same rights and expectations. The Pareto principle allows easy identification of the best use of resources for risk assessment and collection, but it does not diminish the need to meet all customers' requirements. Remember, as someone once said, "big trees from little acorns grow", so *any* customer at *any* time has the potential to be amongst your most important.

So just what are customers' requirements? When looking at any B2B scenario, it is always best to put yourself in the position of the customer as if he/she was a consumer in the B2C environment. In other words, what do you, as a customer, expect from your supplier, how do you want to be treated, and what sort of service do you consider as both normal and acceptable? As a consumer you have expectations of availability, delivery, quality, reliability and service, and your level of satisfaction is determined by how those expectations are met by the supplier, retailer or manufacturer. Whether you buy a refrigerator in a department store, an airline ticket over the internet or a meal in a restaurant, you expect to get exactly what you pay for – the refrigerator works, you have a seat on the plane and enjoy a good meal. Anything less, and your expectations have not been realised. Just as important, remember that as the consumer, you have no interest whatsoever in the internal workings of the service provider or supplier – his difficulties in finding a vehicle to deliver the refrigerator, the slow response of the airline website or the waiter phoning in sick are not your concern.

Think also of the Customer (Big "C") and customer (little "c"). The Big C customer is easy to recognise – he is the one who placed the order and awaits delivery. Who is the little c customer? As credit manager, you are a customer of your own company's internal suppliers – Human Resources, IT, Health & Safety, etc. You expect good service from your internal suppliers (your salary paid on time!!) and your internal customers (Sales, perhaps) expect the same from you. It follows that all contribute to ensuring Big C satisfaction.

Customer Focus

Knowing where you want to be is not just dependent upon knowing how to get there – it begins with knowing where you are now, and that means in order to achieve the goal of total customer focus, you have to understand what makes your business what it is. Understanding your business is the foundation upon which everything is built – people, departments, authority, responsibility, relationships, communications and systems.

People: what motivates people to go to work? Apart from the obvious motive of earning a living, there can be a number of reasons which make people want to work. It may be ambition, the desire to succeed, the need to be with other people, the dignity of making a contribution, the willingness to share, or be part of a team, or it may simply be the fundamental need to earn and survive. Some people care about the consequences of their actions upon others, some are aware but do not care and many are simply totally unaware that what they do impacts directly upon fellow workers.

Everyone has both strengths and weaknesses – establishing a training programme to suit their needs can improve overall contribution, but recognising limitations is just as important. Personality plays a big part in the way people function in the work environment, outgoing or introvert, to lead or to follow, a loner or part of a team.

It does not take long to identify characteristics which point to the motive, and that knowledge can influence the way in which various events can, and should, be handled.

Departments: the way in which any business is structured certainly depends upon its size, and the nature of the business. In small business, one person can have a variety of roles, whereas a large organisation has to be subdivided into departments in order to ensure the totality of the operation: sales, marketing, production, warehouse, distribution, IT, HR, finance etc. Finance may well encompass sales ledger, purchase ledger and credit control – the important point is for all departments to work together to achieve customer satisfaction. In other words, all departments are customer focused.

Authority: Some businesses can be described as being run by the owner, whose word is law. Autocratic management was very much the style in Victorian times, even though the mill owner may have been described in other respects as philanthropic. More comfortable for employees is a management structure which is open to ideas, willing and eager to discuss and debate and come to decisions based upon comprehensively shared information. Such an organisation is also much more willing to delegate both authority and responsibility, empowering junior line managers and staff to take decisions.

Responsibility: see in your organisation whether authority also brings with it responsibility. It is much easier to deal with those decisions taken by people in authority if they are also prepared to accept responsibility for their decisions. Far more worrying is the kind of business that encourages bullying management and refuses to stand up for the consequences.

Ask yourself if both authority and responsibility are clearly defined (here is a central feature of a good credit policy) or if they are merely assumed and accepted. If the former, is that authority, together with its accompanying responsibility, cascaded down through the organisation? Clarity of areas of authority and responsibility are key to a well managed business.

Relationships: central to achieving the goal of all working towards the one aim of customer focus is understanding just how all the different personalities in your company relate to each other – in other words, defining and recognising relationships. They can be confrontational, or co-operative or mutually understanding. In some organisations, people are simply taken for granted, even ignored, whilst in others they can be recognised and appreciated. Knowing the personalities involved eases the task of handling situations as and when they arise.

Communications: how do people communicate with each other? Telephone? Email? Memo? Meetings? Do we walk the floor, talking to each other, or are all contacts hidden behind some communicative process?

Systems: finally, how user friendly are the systems we need to do the work? Accuracy and reliability are paramount when dealing with customers, but equally we need to establish at the time of any change or upgrade what the impact on the customer may be. Ask ourselves – are we upgrading simply to benefit ourselves, or will this enhance the customer interface, and when and if we do change, have we undertaken sufficient training to enable the change to be seamless. Remember, internal issues are of no concern to the customer.

There is more we need to understand – the market we are in, for example:

- Our position in the market place – are we a market leader or one of many providing the same product type or service?
- What is our reputation in the market place – are we well known for our reliability, quality, service, value for money?
- The value of us to our customer – are we a key supplier of something fundamentally important to the success of his business?
- The value of your customer to you – all customers are valuable, but where does he fit in the 80/20 split?
- Your competition – how do we measure up, benchmark and perform? What are they doing that we are not, or vice versa?
- The vulnerability of the market – subject to seasonal or environmental ups and downs, changes in fashion or taste, technological advancement or even changes in local, national and international law?
- Your ability to adapt – one of the most important factors in both success and indeed survival is the ability to change according to market demands and to adapt to new requirements. Can our product or service portfolio be readily adjusted to meet changing requirements?

What is it that we do, and how is it made or provided?

- How is it made? – do we make to stock, or to specific bespoke customer order, or both. Do we rely on sub-contractors for part assemblies, finishing or component supply?
- How is it delivered? – do we utilise our own transport, or use outside hauliers, couriers, packers and distributors? Do we, indeed, use a combination of all these?
- Strengths – it is important that we know what we are good at (manufacturing techniques, perhaps, or innovation)
- Weaknesses – it is equally important to recognise where we have failings (computer systems, perhaps or communications)
- The value to the customer – are we a preferred supplier (ISO9001, Sarbox, etc.), a major component supplier, the only source of a particular product or service, or are we one of many suppliers of similar goods or services?
- The needs of the customer – on time delivery, quality, reliability, price

- The competition – how do we measure up against all our competitors as far as our customers are concerned?

Knowing all there is to know about who we are, what we are, and where we are is the cornerstone of successful commercial operation, and the foundation upon which the credit management function can build realistic and meaningful inter department co-operation, leading in turn to worthwhile customer interface.

Credit Management at the centre
Sales

The definition of credit management, often stated but well worth repeating is “the promotion of profitable sales over the shortest possible time with the minimum of bad debt”. Not difficult to understand (when said quickly!) but often misinterpreted by the omission of the word “profitable”. It is by tradition regarded by many as a finance function – credit management deals with receivables, assessing risk, setting credit terms and credit limits, and collecting resultant debt. That is well known, but less well appreciated by those who do not understand (or are reluctant to try), is the fact that it is not the role of the CM to say no. On the contrary, the task of the CM is to find a profitable yes to every credit application. This may well mean special terms, deposits, interim payments, security or whatever, but only if there is absolutely no alternative but to cash sale or cash with order, will a CM be forced to say no to a credit account.

Working with Sales, the credit function can find the way forward. Too many Finance Directors (shall we call them accountants?) and Sales Directors (shall we call them optimists?) confine themselves to their own KPI graphs – the accountants look at DSO and the sales team look at sales figures. From their perspective, never the twain shall meet. The Credit Manager, however, contributes directly to both, and so draws them together. Ask yourself a simple question of the following, who is doing the better job as CM? –

- When Jack took over as CM in 2008, DSO stood at 62 days against an industry norm of 55 days. Today, DSO stands at 57 days

- When Jill took over as CM in 2008, DSO stood at 62 days against an industry norm of 55 days. Today, DSO stands at 62 days

The question cannot be fairly answered without a piece of vital sales information. Jack’s sales have been fairly flat over the period, going up by 5% since 2008. Jill has seen sales rise by 200% over the same period. Now you can answer the question as to who is doing the better job as CM. It would be true to say that Jack has been highly successful in reducing DSO, but perhaps at the cost of restricting sales and a downsizing of the customer base? Jill, on the other hand, has kept control of the level of receivables against a background of soaring sales.

The point is that Jill’s efforts could only be possible with two way co-operation and understanding between Sales and Credit, and this is perhaps the most important relationship in any business organisation. The cornerstone of that relationship is understanding each other – why we do what we do, how we do what we do, and how we can help each other.

In some ways, it can begin with the simplest of realisations. For the most part, the credit function works in an office – it may be a shared service centre somewhere “remote”, a head office, an office and works on a trading estate and so on. The fact is that the function is “static”, working alongside other colleagues, eating together in the canteen, reading notice boards, gossiping, even going on social events. The sales function, by contrast, is homeless –

the nearest a sales person gets to having an office is his or her car, hotel room, laptop and mobile phone. It may be a fact that it is now easy to keep in touch with what is going on by email, skype, text and all the other modern methods, but any sales person will tell you that it is not the same as sitting in the canteen over a tuna salad gossiping with colleagues about who is doing what with whom, where and how often. Nor is it the same as having the opportunity to debate regularly face to face on issues which are important such as new product lines, system upgrades, redundancies, job realignments and all those topics that keep the noise level in the canteen at a constant hum. Only rarely do all sales people get to "the office" as a group, and that for conferences, sales meetings, target setting and performance reviews. The reason is simple – a sales person in the office and not out on the road is perceived as not selling, and therefore not earning sales revenue for the company. Export sales personnel can be even more remote from reality, being away for weeks or months at a time in Brazil, New Zealand or South Africa – their only contact is by phone or laptop, and the last thing they want to read is a general company email from HR about a proposed change in the pension structure. Put that another way – it may not be the last thing they want to read, but to help them understand it, who in Brazil, New Zealand or South Africa can they talk to? If only they were back in the canteen, chatting over a tuna salad!!!!

Understand the pay structure (this is where motivation arises). In the credit department, apart from perhaps collections incentives or performance bonuses, each staff member, including the CM will know from one month to the next the contents of his or her pay cheque. For the salesperson, remuneration may be more unpredictable, or even precarious – a low basic plus commission, or perhaps a salary related to projected sales and subject to review if those targets are not achieved. Certainty versus uncertainty – understand that ration, and the difference in attitude to sales versus revenue is much more understandable.

There is little mileage in the credit manager simply stating that a sale is not a sale until it is paid for. Sales will see that as being merely dogmatic, and credit in those circumstances is guilty of failing to explain exactly what it means. The cost of credit, and the effect of credit on bottom line profit should be explained simply and without lecturing – even the most die-hard sales person can understand the whole order to cash process if it is set out correctly. The credit manager should be immersed in the sales environment, talking their language, illustrating the cm role and at the same time learning for himself or herself the reality of selling in a highly competitive world.

Language is important in bridging any actual or perceived gap between credit and sales. Credit managers do no-one any favours, least of all themselves, by constant reference to "debtors" – debtors' ledger, debtors' reports and the like. Referring to a customer as a debtor may well be technically correct, and by definition correct, but the word has negative vibes attached. From the sales person's perspective, if the company has made a sale on credit, and payment is not due until the end of next month, then the customer is a customer. It is only when the account becomes due, and then overdue, that the word "debtor" has the significance recognisable, from the sales perspective, as that contained in the dictionary definition. Far better to see the credit function as receivables management and produce receivables reports. When the receivable (customer) becomes a debtor, it is then that sales see that their customer has let them down. It is of course to everyone's advantage that the account is paid to terms, and again the language needs to be modified – part of the education process is for all to get away from the "my customer" syndrome. The customer is "ours", the company's and all are responsible for a satisfactory outcome.

Credit Management at the centre
Queries

The satisfactory outcome extends to resolving customer queries and disputes. It is the matter of query resolution which puts CM firmly in the centre of customer service and brings to the middle all aspects of the business operation. A Receivables report which highlights disputes in DSO terms can be very illuminating to sales and senior management. The credit manager can explain quite clearly what is a profitable sale - one which is priced according to those margins needed to be achieved for success, taking into account the credit period being offered. Any extension to that credit period erodes those margins and there is a world of difference between default and non-payment due to a dispute. An unresolved complaint turns a collectable account into one which is uncollectable. It is not at all uncommon for the CM to be the one who is the final point of contact for the customer, who has already complained to sales, or distribution, packing or production and nothing has happened. Because CM knows the cost of not satisfying that query, he or she has no option to take on the role of customer service and see to it that the matter is sorted out without further delay. It follows that from then on, the CM becomes the focus for customer contact going forward.

Errors are easy to make, and should be equally easy to put right. No matter how efficient a company likes to believe it is, it is only a corporate body, the name registered and the operation conducted from premises. It is in fact staffed by human beings (supported to a greater or lesser extent by machines and technology, themselves produced by human beings), and not surprisingly, human beings are fallible.

Mistakes are many and varied:

- Price
- Discount
- Shortage
- Damage
- Model
- Size
- Colour
- Early delivery
- Late delivery
- Credit terms
- Credit limit
- Wrong delivery
- Special deal arranged with Sales
- Wrong rate of VAT
- Errors in extension
- Wrong address
- Wrong description, or misleading description
- Insufficient details
- Customer order number
- Unable to match to order
- Unable to match to quotation
- Wrong name

Query resolution should never be tackled as a fire fighting operation, but be systematic, methodical and logical. The first task is to identify – the query is logged on first receipt and categorised. Any constant repetition of any one or more from the list above may indicate internal problems which need action – that can be the ultimate outcome. The next step is to prioritise the complaint – the value of the complaint may be small, but it is one line on a multi-line invoice which has a high total value. Settling that quickly releases high revenue potential.

The value of the customer may be such that any complaint, whatever the size, is serious and can have very damaging consequences.

After receiving the complaint and identifying the complaint category, the CM acknowledges to the customer that the resolution process is underway, and takes the appropriate action. That involves whichever of the company departments may be responsible, but also gives the customer the assurance that the matter is being looked into, even if the outcome turns out to be that no credit is required. The customer is also given a realistic timescale for an answer, and that means that the CM has to set the relevant department a deadline by which to respond and resolve. It should also be apparent that no slippage can be tolerated and that the complaint will be escalated to a higher level if no action is taken. In other words, the complaint cannot be ignored – it must be acted upon promptly so that the unpaid invoice can become a collectable item again in the shortest possible time. Experience has shown that a by-product of prompt attention increases the credibility, firstly of the CM and secondly of the business as a whole and can be a major contributor to customer loyalty.

The supplementary outcome of efficient query resolution is the improvement generated internally. Categorising queries determines root causes of internal problems, which may be systems, processes, people or a combination. Once recognised, solutions can be identified and implemented, and that particular problem should not re occur. Equally important is the prompt issue of any credit, if it has been established that the customer is correct and that credit is justified. There should be no argument from sales about this month's figures being adversely affected – whether the credit comes off this month or next month is immaterial, because it will come off in any case. The point is that the sooner the credit is issued, the sooner the invoice can be paid.

A quick glance at the list of potential mistakes as shown above (a list which does not pretend to be exhaustive) is a clear illustration of the number of departments and functions which the CM has to bring together. The Sales/Credit relationship may well be the traditional area obvious to most, but look again at the list – IT, Production, Packing, Warehouse, Despatch, Transport, Accounts, Customer Master File…….. there is no area which cannot escape the need to be customer focused.

Getting it right is the aim, and getting it right leads to satisfied customers. Credit Management squares that circle.