Can you afford not to employ a professional credit manager?

By Kim Radok*

Recently a business owner talking to his credit manager about costs, slow paying customers and very few bad debts, asked in an exasperated voice "Why do I really need a credit manager and to pay for these training courses?"

The credit manager said "To keep the cash coming in to pay the bills and keep you out of jail!"

The business owner said, "Well I am not convinced, but what was that course you wanted to go to again?"

Kim Radok

Introduction

The role of all credit professionals is and has been, to look at the risks associated with making a sale. To understand this concept, you must accept, not every invoice raised will lead to a profitable sale. To paraphrase an old credit saying *"A profitable sale is not a profitable sale until the money is in your bank account within your terms of trade."*

Where past problems have arisen, has been largely due to the historical operational silo operating mentality which existed within large and corporate businesses. In these organisations, a holistic – team like environment does not often exist.

In addition, the reward structures offered for making sales were often not commensurate to profitable sales. More often than not, sales and management were rewarded for raising invoices, but not for timely payment.

In this article, I will focus on the professional credit manager from a risk management perspective. Business today, is being conducted in a world of increasing turbulence and complexity.

It is also not going unnoticed, we are operating in a pre-recession world. If numbers are important indicators of business success or failure, you should recognise that recessions occur on average, every 10 years. As such, the 10-year anniversary of the GFC passed some months ago.

A brief review of today's business environment

Business currently operates globally and where political tensions and the value of globalisation is being challenged by protectionists in almost every country. This has implications, not all good, for every importing and exporting business and their related stakeholders.

Governments and Regulators are increasingly interfering with normal business activities through Legislation, increasing red tape, and associated costs. All of these costs impact negatively on genuine business enterprises and their ability to trade globally. Meanwhile, fraud and the non-payment of legitimate debts are on the rise. The sad truth is, fraudsters and many business people simply ignore the imposts of Government Legislators and Regulators. Finally, the penalties against the perpetrators of fraud and non-payment of accounts are minimal and expensive to enforce.

We also know there are massive amounts of exposed sovereign debt and unquantified hidden business and consumer debt. I would also respectively add, there are many businesses today which have no idea of their liabilities.

It is also increasingly obvious, we are operating in a litigious and regulated world where enforceable responsibilities and penalties are placed on company directors and senior company officers.

The value proposition of employing professional credit managers

As mentioned previously, credit management professionals have many skillsets and different business experiences. As such, they become adapt at

- working in the "grey business world";
- understanding the need to grow profitable sales;
- understanding the responsibilities and fiduciary duties of directors and senior officers of the business.

The grey business world

Unfortunately, despite what many business people think and how they would like to operate, the world of business is rarely a "black and white" affair. It is largely a world of grey where the intersection of rules, regulations, people's needs and desires, plus the MONEY factor, all collide.

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We see clear examples of this "grey business" in selling our goods and services, the payment of our outstanding invoices and the commitment of debtors to repaying their credit obligations.

These business grey areas include recognising the fact that each customer's situation is different. For instance:

- who owns the business and what is the reputation of these owners;
- should the customer be granted credit and if so, how much;
- the customer's payment history;
- is the customer's business, supplier-friendly, i.e. can the supplier's employees operate efficiently with the customer's employees or are there impenetrable walls of technology interfaces which makes this objective almost impossible;
- are there adequate telephone contact details so you can actually speak with the customer's decision makers to resolve issues;
- did the customer raise any issues when signing your business' terms of trade;
- did the customer object to you wanting to register PPSA, directors' guarantees and other security documentation, etc.

The professional credit manager is ideally placed to manage these grey business situations. To operate successfully however, management needs to employ the right type of professional, provide the credit management professional with the resources and authority to operate effectively. Equally important, senior management must learn to respect and accept the decisions of the professional credit manager.

Understanding the need to grow profitable sales

The problem for many business enterprises is finding those customers which lead to profitable sales. There are many potential customers willing to buy. Unfortunately, selling on credit to many of these same customers does not always lead to profitable sales.

Historically, the perception was, credit management professionals would not authorise a sale if there was any perceived risk. This is far from the truth. One of the core roles constantly reinforced for all professionally educated credit managers is; they are to look for all and any opportunities to increase profitable sales.

The problem has always been the differing objectives of senior management and their salespeople verses the credit management professional. Whilst the credit management professional has been employed to increase cashflow and profits, many senior managers and salespeople were motivated to increase turnover to obtain their bonuses. Profitability was rarely a key performance requirement.

On the other hand, credit management professionals are aware that a messy Debtors ledger full of problems, uncollectable invoices and customers with questionable payment practices, requires extra resources to manage. Each of these issues has an adverse effect on cashflow and earnings potential.

In addition, credit professional managers are aware of the issues which exist in today's complex business environment. Each issue, which requires constant vigilance because of its effect on cashflow and profits, include:

- legislation which has led to the emasculation of creditor rights;
- increased costs of legal action to protect creditor rights,
- increased provisions of the Privacy Act,
- the new insolvency laws,
- the Personal Property Security Act (PPSA),
- illegal phoenix activities,
- cybercrime and data storage, etc

These, and other factors need to be accounted for in the battle for business survival and growth. It is the credit management professional which comes across these issues on a daily basis. Consequently, it would seem the educated credit management professional is best placed to help guide their business through such complexity.

The Responsibilities and Fiduciary Duties of Directors and Officers of the Business

Today we live in a litigious world where the merest excuse is used to blame somebody else for your problems. The protections for directors of yesterday have been reduced by legislation and the changing community expectations of what are good business practices. Therefore, with a class action potentially around every corner, nobody is more at risk than directors and the senior officers of the company.

In Australia, two cases against directors for failing to understand and carry out their responsibilities, are I suggest, worth reviewing.

The first was **Morley v. Statewide Tobacco Services Ltd [1993] 1 VR 451** In Morley v. Statewide Tobacco Services Ltd [1993] 1 VR 451, the case involved the role of Executive Directors. In this case, Mrs Morley, a passive director was found liable for the debts of the family business.

The second is **Waterwheel Holdings Limited**

1 *ASIC v Plymin, Elliott & Harrison* (No 2) [2003] VSC 230

2 **ASIC v Plymin, Elliott & Harrison** [2003] VSC 123

In this case, the court found the directors failed to prevent Water Wheel Holdings Limited and its subsidiary, Water Wheel Mills Pty Ltd (Water Wheel), from incurring debts after the companies became insolvent on 14 September 1999.

In addition, the defence of one of the directors was that he had appointed a person to manage the day to day affairs of the firm. It would appear however the director did not keep himself informed of the current situation. In effect, the director appointed an employee to represent him, but did not require that employee to keep him informed of developments.

The Banking Royal Commission in Australia, plus the actions of the authorities around the world against company directors, highlights a number of issues facing company directors today. For instance, bribery, cartel behaviour, ongoing disclosure rules and perceived incompetence when profits are lost are all now front-page news.

Once these issues might have been swept under the carpet and hidden, the offending people quietly paid to go away or sacked. Today, these options are no longer readily available. There is always another aggrieved employee, whistleblowers, investor or finance provider ready to expose and blame directors or senior officers of the business for their losses.

Today, there is almost nowhere for directors to hide from their problems.

This makes the credit management professional even more valuable in today's business environment. They can no longer be thought of a hindrance to sales. The fact is, they help protect the business's cashflow and profits, plus the reputations of directors and senior officers.

In conclusion

The role of all credit professionals is and has been, to look at the risks associated with making profitable sales. To understand this concept, it is wise to realise, not every invoice leads to a profitable sale. At the end of the day, to paraphrase an old credit saying *"A profitable sale is not a profitable sale until the money is in your bank account within expected terms of trade."*

In today's business world, the credit professional credit manager's role includes managing the complexity of issues facing every business. These issues include the loss of B2B creditor rights, increased legislation, changing attitude to doing business and the increased risk of legal action if anything goes wrong.

Finally, the professional credit manager is one the key people which is ideally placed to help protect the reputation and welfare of directors and senior officers. The proviso is of course, that management understands these concepts and is willing to trust their credit managers. ◇

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