
working capital: managing receivables

Five simple steps to creating a functional credit policy

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In brief

Develop a clear credit policy

Many businesses don't really have a credit policy, or if they do, they don't have the right one, or if they have the right one, they don't follow it.

Managing receivables is a key element in business success and is at the core of cash flow management. You might be great at managing the expense side, but what about the income?

Credit policy is not just about collecting money. Having a clearly defined and well-maintained terms will:

- send a signal to your customers that you are a professionally run enterprise;
- enable you to more accurately forecast your cash flow;
- allow you to manage your finances more efficiently;
- help you to handle issues with problem payers.

Make this a priority. You need to have terms and conditions that suit your business and align with the general practices of the industry you are in. It also needs to be monitored. Set up a system whereby overdue accounts are flagged on a regular basis. You need a weekly report showing who is late, who is on time and who is early. Patterns will become clear over time and problem debtors will become apparent.

Make cash flow management a rigorous process. Follow up non-payments. Have definite rules for late payers that follow a definite sequence that calls for a particular action at each stage. Decide at what point you or your credit manager will call the customer requesting payment. On that call, you might offer to waive interest charges if the account is cleared within the next period, but set a date after which the account will not be supplied and after which an administration fee will be charged.



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Be reasonable. Some customers may be going through temporary difficulties and you may be able to assist them with a payment plan. Many will be grateful if you help them through a seasonal fluctuation or an unforeseen development. This will pay off in future loyalty. Don't let it become a habit, but accommodate those cases that you feel are legitimate.

By all means have discussions with problem payers, but once you decide on the next action, do not backtrack. Make each step very clear. If you say you are going to take further action to recover the debt, do what you say.

Review your policy on the pages that follow. Rank your customers and compare your practices with industry standards. Look as well at the terms and conditions of your suppliers. They will give you an indication of how quickly you should be trying to recover what you are due and when.

Most customers will appreciate a clearly defined credit policy. They too need to know what their obligations are. It may mean that some customers will leave. Be aware that you cannot afford some of them. Your customer base will become more reliable if on-going problem payers become other companies' problems. Remember the saying, 'If you lend someone \$50 and never see that person again, the money may have been well spent'.



Step One

Compare how you pay, how the industry pays and how you want to get paid

For example:

WHO PAYS WHAT?	DAYS	SPECIAL CONDITIONS	DISCOUNTS
How you pay: what are the terms your suppliers apply to you?	14 to 90	COD for risk customers	5% if under 14 days
Industry standard: is there a generally accepted policy? What is it?	30	Variable	Variable
The terms you want: what do your cash flow needs require?	14 to 90	COD for risk or special orders	By special arrangement



Step Two

Carry out your own survey

WHO PAYS WHAT?	DAYS	SPECIAL CONDITIONS	DISCOUNTS
How you pay: what are the terms your suppliers apply to you?			
Industry standard: is there a generally accepted policy? What is it?			
The terms you want: what do your cash flow needs require?			



Step Three

Set your B Standard Terms first, then categorise your customers from A to C, then work out your policy

For example:

TERMS AND CONDITIONS	DAYS	SPECIAL CONDITIONS	DISCOUNTS
A Prime Accounts	30 to 90 by arrangement	COD for special orders	By special arrangement
B Standard Terms	14	None	5% for COD
C Risk (or New) Customers	COD	Variable	Variable
Special Orders	COD	Progress Payments	Subject to size



Step Four

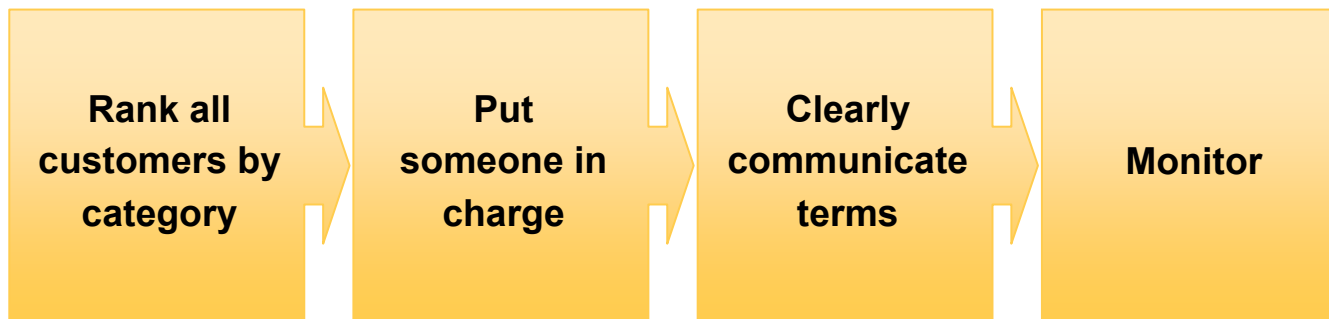
In the template below, set out the terms for your firm

TERMS AND CONDITIONS	DAYS	SPECIAL CONDITIONS	DISCOUNTS
A Prime Accounts			
B Standard Terms			
C Risk (or New) Customers			
Special Orders			



Step 5

Implement the policy



For more information, visit my website www.alanhargreaves.com

Hi, I'm Alan Hargreaves. I specialise in simplifying complex business problems. In over 35 years as a business executive, I have never found an issue that cannot be addressed through identifying the essential but simple steps required to make any problem manageable. It might be your career, your firm, your team or your strategy. It doesn't matter. All hurdles can be lowered through dispassionate analysis, and all executives can embrace simple processes to take them forward.

Using these techniques, I have helped hundreds of people through the various stages of their business or career development. It may be the challenge of taking on new responsibilities; it could be the task of managing a business you have created yourself; it may be handling a difficult team in the midst of major change. I use a straightforward combination of key principles to get results: collaboration, adaptation, simplification and action. You can contact me anytime at alan@alanhargreaves.com.



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