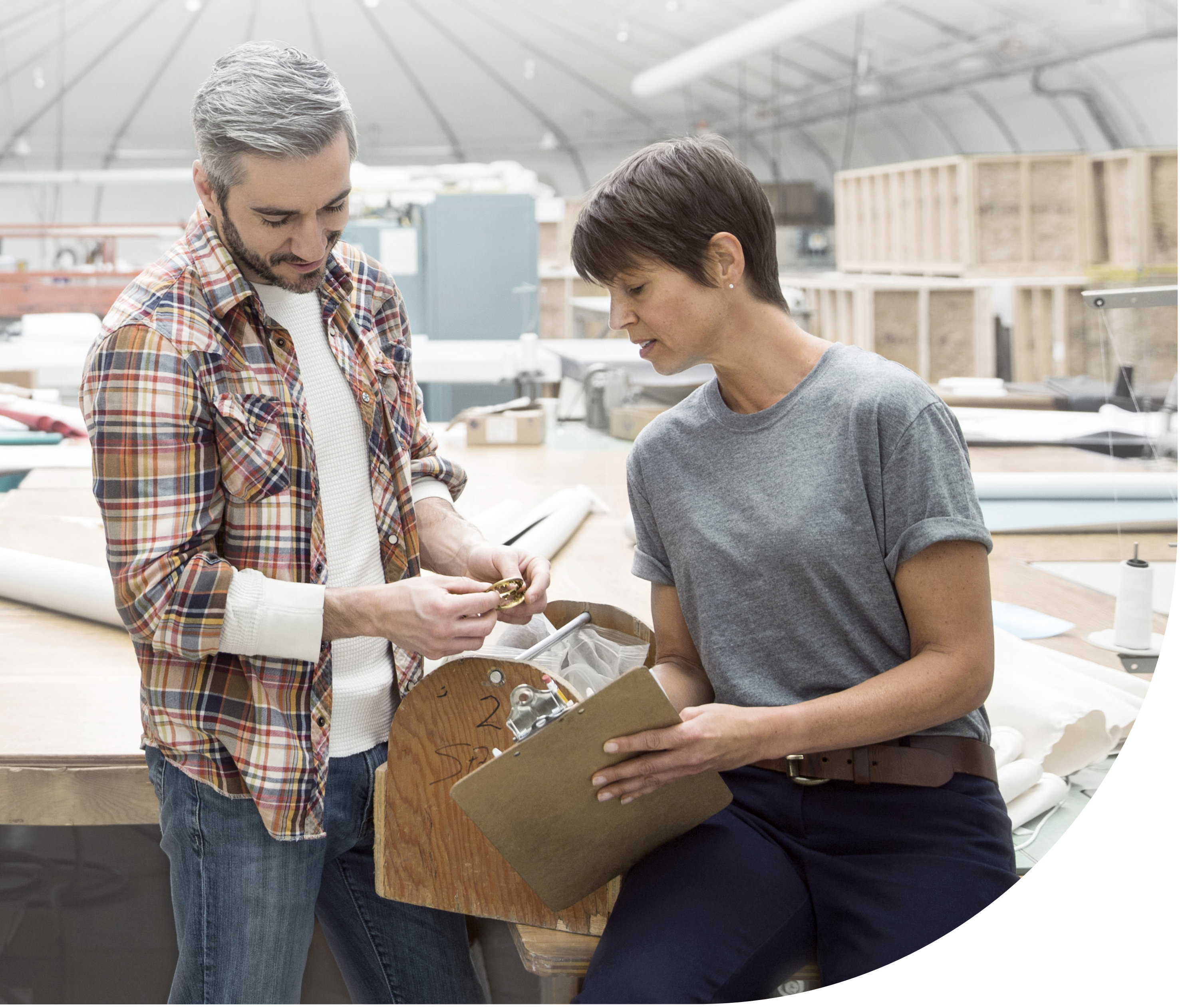
White Paper

The Credit Controller's Guide to Collections



Introduction to This White Paper

Effective credit control can be the difference between success and failure for a business. Get it right and customers and clients will pay their invoices on time, cash flow could be improved and the business will function perfectly well. Get it wrong and the implications could be serious – a lack of money to pay suppliers and bills, and even staff. Long term, the financial health of the business could be put at serious risk.

Follow best practice, however, and many potential issues can be avoided. This White Paper looks in more detail at the credit controller's guide to collections, covering the following:

What is credit control?

- The role of the credit controller
- Identifying risk
- County Court Judgements
- Setting terms and conditions
- Credit management tips
- Day to day management
- Managing problem payers
- Dealing with multiple problem payers
- Seeking legal advice

What is Credit Control?

Credit control is a crucial element in the successful and profitable running of any business. Essentially, credit control is the system used by a business to extend credit only to customers and clients who are able to play on time, and to an agreed schedule.

> “The role of a credit controller is an important one with a specific set of skills and qualities needed.“

The implications of poor credit control are obvious – extending large credit limits to a high volume of customers who may all collectively fail to meet payment deadlines puts the cash flow of the business at risk. In the short term, this could create problems paying suppliers and potentially even employees. Ultimately, being owed significant amounts of money can have disastrous consequences for a business – most drastically resulting in closure and liquidation.

So, the role of a credit controller is an important one with a specific set of skills and qualities needed. In this profile of a credit controller on the National Careers Service website, the following skills are detailed:

- The ability to work to strict deadlines
- Negotiation skills
- The ability to explain financial matters clearly
- Administrative and computer skills

The typical regular and key duties of a credit controller include checking credit records; creating and maintaining customer files; contacting individuals or business customers when payment is owed and overdue; managing and processing payments; beginning legal proceedings if debts continue to be unpaid; liaising with solicitors – and even bailiffs if required – to recover funds.

Clearly, the final stage of those tasks – needing legal assistance to recover money – is the last resort and not a happy situation for anyone. It is not a position any credit controller wishes to be in, but with all the necessary steps taken until that point, hopefully such instances can be limited.

Identifying Risk

No business should enter into a formal contract or financial relationship with a customer or client without doing its homework – in the form of running a credit check. Some businesses may be too focused on jumping at the opportunity to take on every new client, in order to grow their portfolio, to properly check out their credentials first. Failing to communicate properly with a customer and really getting to know them, before agreeing to go into business with them, is a risky tactic, especially if you're thinking of extending credit terms of 30 days or longer. It's a bit like loaning money to a stranger.

Trusting a customer's financial health purely on face value or gut instinct just isn't good enough. Unfortunately, some may not be completely honest about who they say they are and the health of their finances might be in a poorer condition than they have divulged.

Credit checking can help to eliminate uncertainties because a business will be able to get a glimpse of a potential customer's financial status and payment behaviours. Running a credit check on a customer or client can benefit in the following ways:

- **Determine credit worthiness** – to establish whether the customer will be able to maintain payments.
- **Plan ahead** – you'll be able to schedule when you'll receive payments and therefore improve cash flow management and budget better.
- **Determine a customer's longevity** – a credit check will look into the history of the customer. If the business has been in financial difficulty, perhaps even going insolvent in the past, this could well raise a red flag and cause concern.
- **Set terms of payment** – by better understanding a customer's ability to pay, you can then create payment terms which are suitable and have a good chance of being met. For example, if a customer has a poor credit rating you may request payment up front instead of extending credit.

A commercial credit check can help provide the information you need on a potential new client. It includes such information as a company's credit score, limit and rating; repayment histories with suppliers and lenders; the history of the directors involved with the company.

As Experian state here a commercial credit report may be 'one of the most powerful tools a business can have in hand. It's objective, unbiased and timely'.

You can credit check any business with Experian Business Express through a number of tools. This includes Ledger Manager software which shows where outstanding money is and highlights the top debtors to your business. Another service is an identity verification check, which gives a business confidence that a customer is who they say they are.

Sense checking shouldn't be restricted just to customers, either. A business is likely to work with a number of suppliers – all of these should be checked too. What is their financial status? Are they a real business? Is their website genuine? Sense checking suppliers will cover off these areas as well as checking for a County Court Judgements (CCJ). A number of CCJs should be a warning; it indicates the company is experiencing difficulties or perhaps has a history and habit of making payments late – or even disputing them altogether.

With so much insight and data available, there really is no reason to enter into a business relationship uninformed and uneducated.

Terms & Conditions

When a business is satisfied with a customer's credit rating, it can proceed to the next stage – setting and agreeing the terms and conditions of the arrangement. This is an important part of the procedure. It's an information gathering exercise and also the opportunity to set rules in place for the duration of the relationship.

This is when a business takes a decision of extending credit, how much and for how long.

A business may not decide to offer any credit at all, in which case any alternative payment arrangements should be discussed with the customer.

Start Up Donut has a really useful checklist, which includes:

- Setting a maximum credit limit for each customer
- Giving new customers a modest credit limit in the early stages – which can always be increased once trust is earned
- Consider taking out credit insurance
- Consider how much you can afford to risk losing

The credit terms you are willing to extend compared to the terms you have with your own suppliers – in other words, do you have to pay your supplier sooner than your customers pay you?

A business could consider including upfront payments too, with new customers, and also possibly introduce a discount for early payment (though it's important to note that this wouldn't affect credit rating).

As well as the size of credit being extended, how long a customer has to make payment is important, too. For example, payment terms may state a customer has 30 days to pay an invoice, others may push for longer at 45 days. Alternatively, a business may operate on payment terms of 14 days only and make no exceptions.

A business may also decide to include terms of claiming interest on late payments – which will be covered in more detail elsewhere.

Whatever the length of these payment terms, a business must ensure it can operate and survive financially during the times between being paid. Once these terms have been agreed, they should be signed by all parties – remember, terms and conditions are there for the benefit of everyone.

Credit Management Best Practice

With all credit and status checks complete, and terms and conditions drawn up, agreed and signed off, many potential issues will have been covered off before business starts properly. All being well, the relationship will run smoothly, amicably and professionally but this isn't always the case, unfortunately.

Sound credit management starts from the very first invoice sent out, and the skilled credit controller has to be flawless in this aspect. It's important to invoice promptly and accurately, ensuring the paperwork is addressed to the correct contact, and that full bank details are included as well as the nature of the work being billed. An agreed payment date should be clearly visible, too.

Some businesses won't pay an invoice unless there is an order number attached to it, so establish this before sending. In addition, some businesses – particularly larger ones – have an organisational structure that dictates invoices must be received and authorised by a set date every month in order to meet the payment run.

The credit controller should confirm what this date is and ensure the invoice is despatched in good time – it's little use sending an invoice out on the 20th of the month if the business in question has an internal payment run on the 18th.

Effective credit control is an everyday task. The credit controller should set aside some time every day to review the status with invoices – including calling the named contact to confirm receipt – check the outstanding credit across the business, and start chasing payment as soon as any account becomes overdue.

Managing Problem Payers

Inevitably, some customers will either make payment later than agreed in the terms and conditions or not at all. Problem payers can be difficult to manage, but these are the instances when the credit controller really proves his or her value to a business. It's their job to collect the money owed.

A system for chasing debts should be implemented and adhered to. How quickly a business should chase a payment after the due date has expired is a decision for the credit controller but certainly a week late is time for action.

At that stage, it's time to get in touch with the customer; ideally by email and via a telephone call. Stay polite and professional, and try to establish why there has been a delay and receive confirmation on when the invoice will be paid.

The credit controller is likely to be given a few reasons for non payment, some of which are detailed here. It's important to be prepared for such common responses and primed with a follow up – just in case the customer is stalling.

For example, if the customer promises to look into the matter and call you back, request an agreed time for the call rather than just letting them call back when they choose.

If the customer insists the 'cheque is in the post' – which is a possibility, despite it sounding like a weak excuse – then ask for some details; cheque number, date it was sent and so on. This will help to identify it when it arrives, or alternatively highlight it as just an excuse.

Apply the same approach to any replies at this stage of chasing payment – ask for extra detail and don't accept anything at face value. Ensure the customer at the other end of the phone is aware you'll be in touch again, and relatively quickly. Make a record of any conversations to refer back to if required. Be friendly but persistent and don't apologise for chasing up money that the business is owed.

If the invoice remains unsettled, after the first round of chasing for payment, clearly you will have to escalate actions. Communications in writing should be stronger and firmer in tone. If you're having continued problems getting hold of the named contact, vary the times you call.

If the situation continues to a point deemed unacceptable – 30 days past the payment date might be considered seriously overdue – then the cash flow of the business is put at risk. At this stage, more serious action might have to be taken. Until then, the business could at least ensure it no longer provides any goods or services to the customer. Don't allow additional credit and place the problem payer customer on 'pause' until the outstanding invoice is paid.

> “How quickly a business should chase a payment after the due date has expired is a decision for the credit controller.”

Managing Problem Payers

Of course, there's a good chance a credit control department will be dealing with more than one problem payer, perhaps chasing several customers. In these instances, it can be difficult to know which customer to prioritise

This scenario might prove helpful if you do encounter such a situation:

Imagine you have two clients – both owe you money. One of them owes £1,000, and the other owes £5,000. Which outstanding invoice should be chased first? Most people would probably assume the larger debt – £5,000 invoice – should be given priority but a look at the respective credit histories of each of the customers might provide a different picture. If the customer owing £5,000 has a track record of usually paying on time, or within a reasonable period at least, and has an excellent credit rating, then it's not necessarily such a concern.

However, if the £1,000 customer has a really poor credit rating, bad historical payment records and looks in danger of going into liquidation, then this is the invoice at risk of going unpaid. Therefore, it's worth the credit controller chasing this first, even though it is a smaller amount.

Late Payment Legislation

As mentioned previously in this guide, businesses do have a legal right to charge interest on payments received late, under the Late Payment of Commercial Debts (Interest) Act 1998. This was later revised in 2002. Whether to enforce this or not is a decision for each business to consider. An interest charge of 8% plus the Bank of England Base Rate can be applied from the first day that the debt is overdue. There are more details on the legislation included here on GOV.UK and here on legislation.gov.uk should you wish to learn more.

Problem Payers – Recovering Debt

Despite the best efforts of the credit controller, there will be instances of invoices being unpaid even after several rounds of chasing. When matters cannot be resolved amicably, it is time for a business to look at other ways of recovering the outstanding money. As covered in this credit control guide there are three main options.

A business could employ a debt collecting agency, but they have to be reputable. Collection agencies should be registered with the FCA – Financial Conduct Authority – and belong to the Credit Services Association. Using an agency to aid in the recovery of funds will speed up the process of collection and also remove the burden from the in-house credit controller. Make sure you choose the right debt collection agency; not only reputable but one which will maintain the relationship with the customer and not alienate them

Another alternative is to turn to a solicitor and begin legal proceedings. What usually precedes this action is sending a letter of claim, which really starts the legal process. The letter can be written by the credit controller as it simply states the situation – there is a template for such a letter on the Which? website. A letter of claim typically provides a summary of the facts so far, what you are trying to collect from the owing party, documents to help support your cause – which could be a record of communications – and a deadline for a response or payment. After this, you may receive payment. If not, the letter is a statement of intent to sue and you can then direct your legal representation to take up the case.

Bear in mind, of course, that going down the legal route could be expensive.

A third option is to engage legal proceedings but conduct it yourself, without engaging a solicitor. You can take court action against someone who owes you money and make a money claim online. To do so, you will need a Government Gateway ID and the submission process takes around 30 minutes.

Making a court claim and using legal representation to collect monies owed to the business should be the last resort in this process. Ultimately, it should end with you being paid what you are due but will almost certainly conclude with you losing the customer in the long run. It's unlikely you'll ever establish a professional relationship again. If you can reach a satisfactory conclusion before this stage, all parties should see the benefits.

Credit control is not an easy job – it requires organisation, persistence, professionalism, understanding and a thick skin! But by having set procedures in place and following them through, step by step, you can minimise any risk and financial losses, improve cash flow and therefore the success and smooth running of the business.

Further Reading & Useful Contacts

- Credit Control Guide by Crunch
- Experian's Credit Check
- Chartered Institute of Credit Management
- GOV.UK
- Startup Donut
- The Business Index
- HSBC

Sources:

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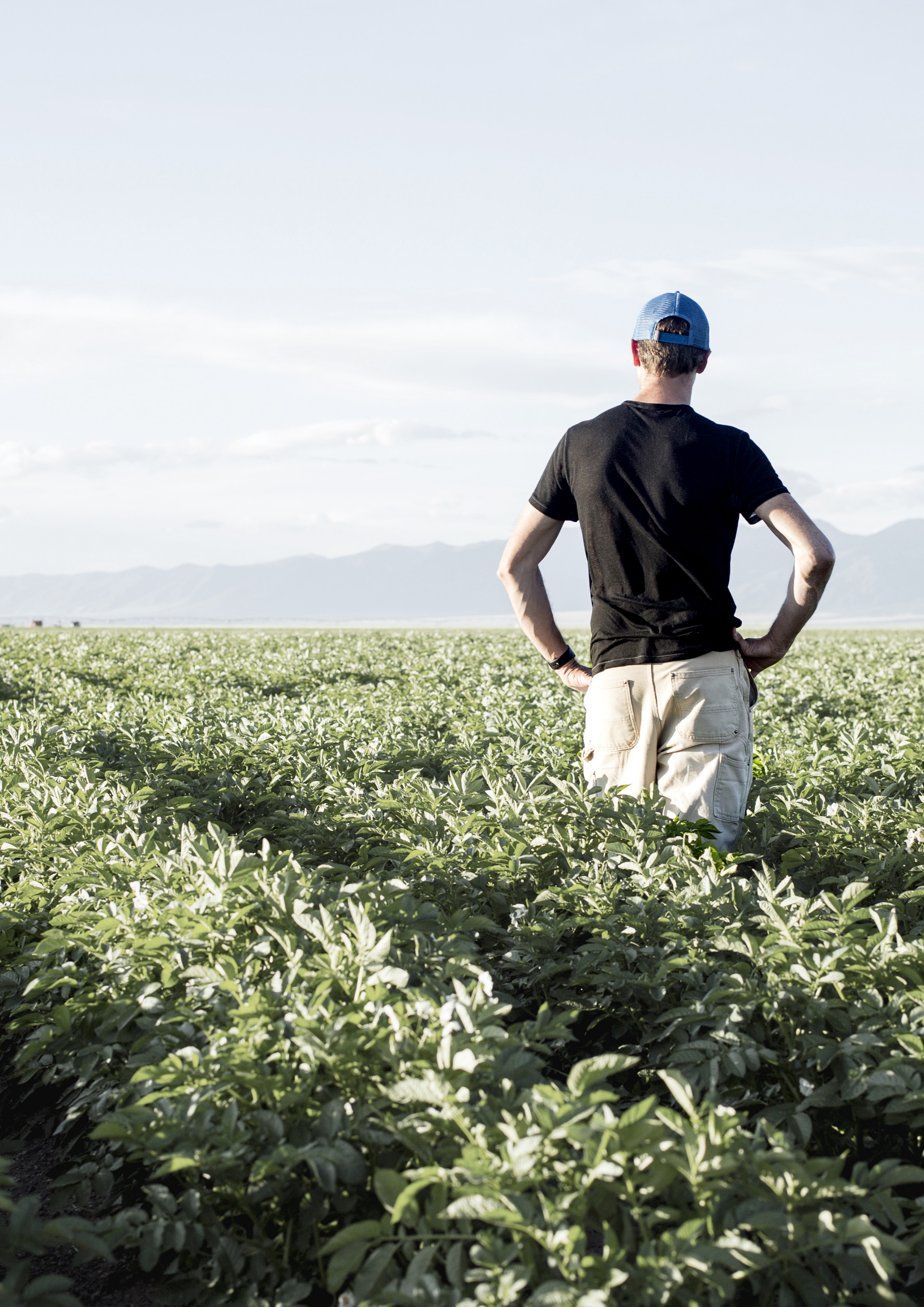

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