



ADVISORY

ACCEPTANCE & COMMITMENT EQUAL IMPROVEMENT

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"Employees respect (do) what managers inspect (measure) and not what managers expect."
— Don Rice, Distribution expert and former Texas A & M University professor

Make a list of your top three assets (your business assets, not your wonderful smile or engaging personality):

- 1) Asset _____ How much? _____
- 2) Asset _____ How much? _____
- 3) Asset _____ How much? _____

Is the A/R, short-term money due from the sale of a product or service based on delayed payment, on the list? If it is, you are not alone. On average, the A/R makes up 40% of total business assets. A/R is often one of, if not *the* largest, asset a business has.

If the A/R asset in your business is not in the top three ask yourself why not. Is it because you are the sole source for the product/service you provide and therefore you can demand and get payment in advance? You own your customers and they haven't any other place to go? Or if you have unused capacity, i.e. the ability to take on more business without additional fixed expenses, is it because you aren't using credit to its fullest profit potential?

Your expectation and inspection

What do you expect of your credit function – that area of business which creates and manages the A/R? All human activity must have a starting point and a direction. What is your starting point for your credit area?

Do you believe that the role of credit is *risk mitigation*, that it's about avoiding bad debt losses and making sure customers pay when they're due? If so, you probably inspect for DSO (days sales outstanding) and percent bad debt. Use of *risk mitigation* measurements com-

Abe WalkingBear Sanchez is president of **A/R Management Group, Inc.**, a consulting and training organization specializing in "profit-centered credit" with A/R management. STAFDA members may receive 30 minutes of free phone consultation with Abe each year. He can be reached at PO Box 457, Canon City, CO 81215; phone 719/276-0595; fax 719/276-0594, e-mail abe@armg-usa.com; website www.armg-usa.com

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municate to the credit staff, or to the credit part of your brain if you are a one man band without a separate credit function, that the job is to qualify new potential customers based on risk alone and to stop selling to those who fail to pay when due.

Or do you expect the credit function, or the credit part of your brain, to take into consideration:

- 1) The customer's profile (who they are and how they do business),
- 2) Their past performance (credit report), and
- 3) Your product value at time of sale (margin, demand, capacity)

And then find a way to make a profitable sale while remaining confident of payment through the creative use of terms and conditions of sale?

If you expect your credit function to take a wide profit-driven view of the job and measure for risk (DSO and bad debt) you're kidding yourself and confusing the credit staff.

Acceptance

For improvements in business to take place, it requires an acceptance that a business doesn't have to be sick in order to get better. There is always room for improvement.

If you are inspecting for risk, chances are that's what you'll get. If you inspect for profit, chances are better that it's what you'll get.

Instead of seeing credit approval as a fear/risk-based activity, start thinking of it as a *pending sale*. Consider the investment you've made to finally get a potential customer to the point where they want to buy. Your whole reason for being in business is represented by that Customer Credit Application, or better still a New Customer Information Form. Someone wants to buy from you.

Tell your credit guys the goal is to find a way to say "Yes" to profitable sales while remaining confident of payment via credit terms and conditions of sale. Tell them you will be inspecting for the *percent of applied for dollars approved or exceeded*.

Tell your staff most past due customers are not trying to avoid payment and the job of past due A/R management is not collections (the enforcement of payment) but rather *the completion of the sale*. The goal is to find out what's keeping a customer from paying and resolve the issue so the customer can buy again.

And yes there will be a small percentage of past due customers that represent a potential for loss, so tell your people the secondary goal of past due A/R management is to identify the small percentage early on to improve on your position for payment. If they refuse to cooperate, refer them to a "collector" – an enforcer of payment.

Tell them you will be inspecting for the percent of the total A/R current to 30 days past due and also for the percent of the Total Credit Line being used. *Total Credit Line?* The total dollar amount of the combined lines of credit (never credit limit) for all credit customers.

Commitment

Acceptance is one thing but putting energy into change for the better is the true test of desire for change, for improvement.

Where is your credit department located? Who within the organization do they report to? If you are using the accounting part of your company to house the credit function, you need to consider moving it to the sales area. Why?

- 1) The reason why the costs of credit (additional administrative expense, time value of money in carrying A/R, and potential loss) are incurred is to get profitable sales that would otherwise be lost.

2) Past due A/R management is the *completion of the sale*.

The financial part of your organization must maintain oversight of the credit function as part of its role of safeguarding business assets, but credit is a sales support function and should be found in and reporting to sales, not accounting.

Improvement and Profitability

There are several ways to enhance profitability in a business. First there is the *Enron Model* which consists of cooking the books. One of the possible downsides to the *Enron Model* is that you may end up in jail.

You can also improve profitability by selling more and taking advantage of the economy of scale. In production, the reduction in unit cost resulting from increased utilization of the method of production leads to efficiencies as the cost of producing each additional unit falls. The same is true of sales. Sell more without increasing fixed expenses and the unit cost per sale drops.

Another method for enhancing profitability is to reduce the cost of doing business. While there are several ways of reducing costs, such as downsizing people, the best way is by constant and ongoing improvement.

On average, 25% of the Total Cost of Doing Business is tied to inefficiencies: the waste of time, energy, or materials, and missed opportunities. Many CEOs will tell you they think that 25% is on the low end.

The credit function while approving credit and managing past due A/R interfaces with new potential customers, existing customers, sales, finance, the warehouse, accounting, operations, attorneys, transportation companies, and others within and without an organization. The credit function is in a prime location to identify and communicate *areas of opportunity for improvement* which lead to reducing the cost of doing business for the seller and customer alike.

It may not be so in your company, and if it's not, be happy. But in too many businesses, employees and business managers repeat how things are done over and over again until it becomes engrained. And all too often CEOs and top management are complicit if not directly responsible.

If you are a business manager, pull out your job description. If you're a CEO, pull out your managers' job descriptions and check to see if it/they say anything about "Constant Improvement".

Change Management

For change/improvement to take place, there must be a commitment made as to who will do what, why, how, and when...and then the efforts must be tracked and measured.

Change, even for the better, generates resistance. Expect it in others and in yourself. Keep change small so as not to overwhelm others or yourself but once one change is in place, bring in another small change/improvement.

Pay for what you want. Measure the correct performance and pay your staff to achieve the goal.

A small increase in sales or a small improvement in how business processes are carried out will have a dramatic impact on profitability.

Consider a Friday afternoon "Improvement Meeting" and at the end of the meeting organize and prioritize what has to be done first on Monday. This should be done for all business functions.

Before improvement/change for the better can take place, two things must happen: First, there must be an acceptance or acknowledgement that a business doesn't have to be sick in order to get better. Then someone, a profit leader, must step forward and do something about it.