

Credit Policy Boot Camp – Part 1

Critical Information Every Credit Policy Should Contain

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Housekeeping...

My knowledge & perspective:
36 years – Credit & Finance Profession
25 years -- Lumber industry

“Interactive” Session – PLEASE share your thoughts & ideas –
We all benefit from the exchange of information

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Objectives

- What Is A Credit Policy?
 - Why Is It Important?
 - Function / Purpose
- Rules, Procedures, Guidelines
- Critical Information / Details
- Realistic / Relevant / Timely
- Management Buy-In & Approval

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What is a Credit Policy?

By definition (taken from the Principles of Business Credit) ...

An effective credit policy permits and encourages the fullest development of the opportunities in administering credit. It provides the latitude to plan departmental operations within the scope of the company policy, **while creating effective procedures and techniques to implement that policy and establish adequate controls.** It can assure that there is consistency in the company's dealings and interactions with its customers and it provides a means of recognizing the importance of the credit function to the company.

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What is a Credit Policy? (continued)

- Your company's credit policy should include a procedure, or series of steps, to be followed on a consistent basis, for recurring credit situations, to help your credit team assess acceptable levels of risk and set guidelines for establishing:
 - Customer Credit Limits
 - Terms of Sale (based on class of business / industry)
 - Credit File Documentation / Monitoring
 - Collection Procedures
- NACM – Resource Library, White Papers, Network, Industry Groups, Peers, Colleagues, Mentors, etc.

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“Poll The Audience”

- Does a credit policy exist at the company where you are employed?
 - If yes, have you read it?
- Have you been adequately trained to understand & implement it?
- If no, were you influential in creating your company's credit policy?

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Credit Basics...

- A sale isn't a sale until it's been paid for.
- Credit's primary objective – help our company maximize profits and minimize losses
- Often times, trying to find credit information to justify and support saying “Yes” to the Sales Team
 - The ‘big picture’ – The cost of doing business.

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Critical Information - Components

Policy Objectives – aka Mission / Vision Statement
New Accounts – Required Documentation
Existing Customer – File Review Documentation
Terms of Sale
Calculation of Credit Limit
“Hard Stops” / On Hold Parameters
Contract Requirements / Terms & Conditions
Liens / Bonds (if applicable)
Collections / Legal Action
Terminology / Definitions

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Policy Objectives – Mission / Vision Statement

*Summarize Objectives / Parameters detailed within policy

*Define Credit Policy's Purpose & Intent

*Steps, Procedures, Guidelines to be followed

*Consistency in Decision Making

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New Accounts

- Required Documents in your Credit File:
 - Credit Application Document(s)...
 - Credit Application
 - Terms & Conditions
 - W9
 - Sales Tax Exemption Certificate
 - Personal Guarantee
 - Bank Authorization

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New Accounts

(continued)

Credit Investigation –

- *Trade References – How many? Meaningful...
- *Bank Reference(s) – Depository, LOC, Loans
- Anything 'derogatory'? NSF activity, perhaps?
- *Agency Report(s)
- *Notations of any Public Record – Liens, Suits, Judgments
- *Financial Statements – Depending on sales exposure & risk

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New Accounts

(continued)

Credit Investigation... more detail

- *Tie Legal Business Entity to Federal Tax ID number
- *Internet Search / Social Media
- *Credit Insurance Coverage (if applicable)
- *How Long in Business & Type of Business
- *Pay History

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Existing Customers – File Review

- Define Parameters Required for File Reviews/Updates
 - How often?
- How much information is required for audit compliance?
- Is your 'file review' predicated on other parameters/requirements, i.e. the continuation of Credit Insurance Coverage?
 - Changes in Business Entity Structure or Ownership?

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Existing Customers – File Review

- Corporate 'Umbrella' – Sharing Current Credit Information?
- Summary – note any changes in credit documents or pay history
- Does updated credit information necessitate Credit Limit Adjustment?
 - Document changes...

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Terms of Sale

- Define 'Standard' Terms, based on your industry
 - Discount? Yes or No
 - Define customers by:
 - Business classification / SIC code
 - Products being purchased
 - Industry Standards

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Calculation of Credit Limit

- Credit investigation & review of results
 - Credit Insurance Coverage Criteria
- Length of Relationship & Customer Integrity
 - How Long in Business & Type of Business?
 - Pay History
- Terms of Sale (Must document & support non-standard)

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“Hard Stops” – On Hold Parameters

- Credit Report reflects consistent slow pay activity
- Credit Report notes open/outstanding derogatory public record detail (liens, suits, judgments)
 - Inability to qualify for credit insurance coverage
- High credit balances (on credit report or trade references) do not match or exceed value of pending sale(s)
 - Lack of Credit Information – example: New Business/Entity
 - **Past Due Balances within our Corporate Organization**

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Contract Requirements / Terms & Conditions

*Contracts –

Review Thoroughly

Make Sure Both Parties Agree

Define who has Authority to Sign

*Terms & Conditions –

Define steps or processes if your document is modified

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Liens & Bonds

- Based on 'Who is your Customer', Product being sold, and Scope of work/services being completed
 - Define Parameters and set reminders regarding Notice and Filing Dates

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Collections / Legal Action

- At what point are you expected (or required) to request assistance from a collection agency or legal team to help collect debt owed to your company?
 - This parameter can be much more difficult to quantify, based on payment commitment & communication from your customer
 - 10 Day Demand
- When do you write off balances to bad debt?

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Terminology / Definitions

- Example: Definition of Credit 'Exposure':
- Credit Exposure represents the shipped and invoiced balance open on each customer's account (Open A/R). This does NOT include confirmed but unshipped orders, pending orders on credit hold/control, or payments 'in the mail' even if backed by customer pay history and integrity.

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"Realistic/Relevant/Timely"

- Do current parameters in your credit policy make it difficult to meet audit requirements?
- Example – Three Completed Trade References; how many do you request? Do you receive responses from everyone?
- Are existing credit limits 'realistic' during unprecedented market condition swings?
- With constant technological advancements, is it timely or realistic to require hand-written completed trade references on company letterhead generated reference request forms?

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Management Buy-In & Approval

- Determine how often you review your credit policy.
- All 11 operating company Credit Managers meet with Corporate Credit Manager to discuss policy/procedures.
- We all have a voice in recommending changes, discuss, and vote as a collective team.
- Before ratified & published, approvals required of each operating company controller and President.

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Conclusion...

- Your company's credit policy should be an extension of your efforts to effectively manage the risk and credit exposure for your business.
 - A written credit policy will help you make decisions fairly and consistently.

Determine the 'Critical Components' that should be well defined in your company's credit policy

Document your policy requirements, procedures, and guidelines

Review periodically to ensure they are realistic, relevant, & timely

Ask for Management Buy-In & Approval

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Conclusion...not quite done yet

- Create or Modify a credit policy that best suits your company, products or services provided/sold, following industry specific norms and expectations.
 - No two credit policies should ever be identical
- Create a list of critical components that are consistent for every credit decision you make to include in your credit policy
- Engage your network of colleagues & peers, especially within your own industry

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Questions / Comments

• *Thank You!!!*

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