

# Credit Policy and Procedures Part 1

- Presentation by Debie Wangsgard, CCE



Credit Policy and Procedure Manual

A credit policy establishes a framework or guide for consistent credit decisions.

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Learning Objectives

- Components of a credit policy
- Steps used in establishing a credit policy
- How a credit policy is implemented
- Why periodic reviews of your credit policy is important
- Difference between a Policy, Procedure, and Rule
- Types of credit policies
- Components of a credit manual



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

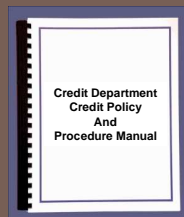
---

---

---

## Creating a Credit Policy

- Define
- Establish
- Implement
- Review



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Defining Credit Policy

The credit policy for the company must be in harmony with the Goals and Objectives of the company and should support sales initiatives.



An effective credit policy permits and encourages the fullest development of the opportunities in administering credit.

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Policy vs. Procedure or Rule

- **A Policy** is a general course of action developed for recurring situations and designed to achieve established objectives.
- **A Procedure** is the actual working steps that should be followed in an appropriate order to accomplish a desired result.
- **A Rule** is a statement that defines or restricts the actions that a credit professional can take or not take in a specific situation or decision.

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Example of a Policy

- Bad debt will be reviewed and written off quarterly
- Bad debt must be submitted by the Market Credit Manager for approval prior to the debt being removed from the A/R
- Bad debt is defined as any account balance that is deemed uncollectible for the following reasons:
  - Business closed
  - Owner skips
  - Bankruptcy
  - Death of the owners of a sole proprietorship

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Example of Procedure

- Bad debt will be submitted by the market credit manager to the Corporate Credit Manager for approval no later than the 24<sup>th</sup> day of March, June, September, and December.
- Approved Bad Debt will be keyed off the A/R by the last day of each quarter.
- Bad debt is coded to General Ledger number 100.9948.100
- Back up for all bad debt must be kept in the customer credit file and added to the Bad Debt tracking log. Backup must include a copy of all invoices that will be written off, a statement showing the total amount due and aging of the account. Also include copy of all collection notes, and a copy of the signed authorization from the Corp credit manager.

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Example of a Rule

- Only Market Credit Managers can key a bad debt batch in the system.
- The Corporate credit manager has authority to approve bad debt up to \$500,000. Amounts over \$500,000 must be approved by the CFO.

NACM Credit Learning Center

---

---

---

---

---

---

---

---

## Company Defined Objectives

Goals Both Long Term and Short Term



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Objectives of a Credit Dept.

Terms of Sale

Training & Development of Credit Personnel

Amount of Capital Committed to A/R

Monitor Risk

Relationship to Sales Dept.

Measurement of A/R Investment

Credit policy should address the authority to do the job, establish consistent credit guidelines, and incorporate credit and sales cooperation.

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Handling Exceptions

- ❑ Credit is not black and white
- ❑ Need some Flexibility
- ❑ How will exceptions be handled?
- ❑ Who can authorize exceptions?
- ❑ How will they be documented?



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Scope of Credit Policy

P  
O  
L  
I  
C  
I  
E  
S

- ❑ Purpose, Plan, Performance, Performance Measure, Preparation, Productivity, Positive Results
- ❑ Organizational Expectations (goals/objectives)
- ❑ Level of Understanding, Limit of Authority
- ❑ Investment, Impact, Individual Responsibility, Individual Department Needs
- ❑ Corporate Goals and Desires, Credibility, Consistency, Chain of Command, Cooperativeness
- ❑ Intentions, Important Points, Instructions, Implementation, Innovation
- ❑ Established Ground Rules, Employee Training Manual, Effectiveness, Employee Input (sales, service)
- ❑ Stability, Sensitivity, Support, Security, Standardization, Strategic Planning

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Establish Credit Policy

- Because Credit Policy affects the company as a whole, it is usually formulated by top management.
- It must be in harmony with the goals of the company
- It must be trained to more than the credit department

---

---

---

---

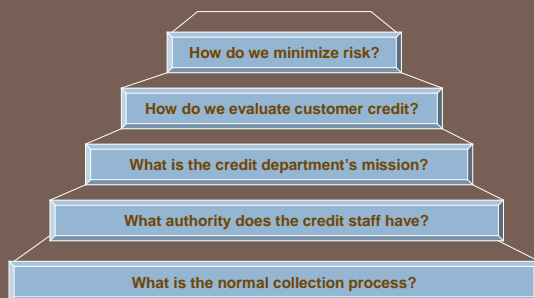
---

---

---

---

## Steps For Establishing Credit Policy



---

---

---

---

---

---

---

---

## Credit Policy Focal Points

- Development of an optimal level of sales
- Minimize the carrying costs of receivables
- Minimizing bad debt losses
- Credit department organization and cost containment



---

---

---

---

---

---

---

---

## Develop Optimal Level of Sales

- When do you need credit applications?
- Expected time to make a credit decision
- How will decisions be communicated?
- Who will establish and maintain credit files?
- Who can authorize credit limits, raise limits, lower limits?



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Terms of Sale

- What will terms be? (What terms does your industry use?)
- Who will communicate them internally and to the customer?
- Who will apply and monitor discount charge-backs?
- Who will apply and monitor late payment service charges?
- How will requests for extended terms be handled and who can authorize them?
- What happens if a customer files bankruptcy?
- Blanket Order approval
- Orders that go on hold because the customer is past due or over their credit limit

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Credit Investigations

- Sign off policy for approvals or denials
- What credit reporting agencies and credit reports will be used?
- Will you require bank references and trade references?
- Will you require financial statements?
- Will you take Collateral?
- Will you perfect liens under Article 9 of the Uniform Commercial Code?
- When will you require personal guarantees?
- Will you file Preliminary Notices and Liens (construction industry only)?

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Minimizing Carrying Costs of Receivables

- Responsibility and time intervals for follow up of past due accounts.
- Holding orders
- Handling deductions
- Exchange of credit information
- Cash application
- Handling deductions
- Placing accounts with 3<sup>rd</sup> party collections
- Bad debt write-offs
- How will progress of collections be monitored?
- Employee travel and expense reports

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Internal Reports

- Aging report
- Over the credit limit report
- Reports to monitor: unearned discounts, deductions, unpaid service charges, credits.
- Reports to track accounts placed with outside collection agencies or attorneys
- Bad debt write-off report
- Travel and Expense reports



NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Minimizing Bad Debt Losses

- Conversion of an open account to a note
- Customer counseling
- Collection agencies
- Use of outside attorneys and lawsuits
- Customer bankruptcy, bulk sales and assignments for the benefit of creditors.
- Authorization for accounts written off to bad debt

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

## Credit Department Organization and Cost Containment

- Formal organization chart that defines positions and authority of each credit department associate
- Hiring guidelines
- Educational requirements by position
- Experience requirements by position
- Training and development guidelines
- Performance review criteria
- Promotion and termination guidelines
- Credit department budget guidelines
- Collection policy that reduces borrowing costs and generates cash flow

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

---

---

## Influences on Credit Policy

- Competition
- Classes of customers
- Financial standing of the company
- Length of terms
- Type of merchandise
- Price range of merchandise
- Profit margins
- Economic conditions

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

---

---

## Implementing Credit Policy

- Communication of Policy Both Inside and Outside the Credit Department
- Assignment of Responsibility or Authority
- Establishing Procedures, SOP's, Job Descriptions

NACM Credit Learning Center

Credit Policy

---

---

---

---

---

---

---

---

---

---



# Credit Procedures Manual

- Should cover rules, regulations, and procedures necessary for consistent department operation.
- Credit Manual may be a separate book or part of a general company instruction manual.



---

---

---

---

---

---

---

---

To be continued with next learning module:

## Part II Credit Application

---

---

---

---

---

---

---

---