Red Flags That Warrant Consideration for Renegotiating Terms

Every day that a B2B payment is late, the value of that receivable to the creditor declines. What's worse is that if a late payer ends up in bankruptcy, it takes the rosiest-colored glasses to hope for more than pennies on the dollar.

Spotting negative warning signs and trends among customers in advance of troubled waters, such as insolvency, is critical for credit managers. If enough red flags are in play or a couple are massively troubling, it is imperative to ensure that the open terms on which the customer is buying are not too lenient. If negotiating changes to an existing non-contractually bound situation, doing so more than three months in advance is so important. Remember: changes to payment behavior within the 90 window before a filing can mean preference claims in court by other creditors—This can, and has, resulted in trade creditors being told by a judge they must to give the money back to a bankruptcy trustee with little hope much of it going to unsecured creditors.

The following are some warning signs for which to look:

Industry on the rocks. Looking at the colleagues/competitors of one's key customers can be beneficial in that, if many of their rivals are falling on hard times, it could be an industry-wide phenomenon. For example, after years of massive success and very low bankruptcy levels, the oil and gas industry suffered a spate of Chapter 11 filings, large and small, in 2015 and 2016. As the price of oil continued to fall and a glut of supply kept worsening as more and more companies entered the subsector, times suddenly got very tough for those in oil production and the material suppliers that serviced them. Many in the industry were damaged worse than was needed simply by being unprepared.

Cooled relations. A tried-and-true adage in trade credit is that strong relationships are paramount. So what happens when the relationship with a longtime friendly customer inexplicably becomes strained (e.g., odd communication exchanges, refusal to respond to a call or email, avoidance at events like conferences where you'd previous spent time together, etc.)? It should send off a proverbial warning bell. Perhaps it's nothing; but discreetly performing a little due diligence on things like financials or how the customer in question is paying others (which can be ascertained at NACM Industry Credit Group meetings) can't hurt.

Changing payment type. If a customer has a long history of paying by a certain method and, without explanation, asks to switch to another, it could be innocuous. However, it is worth following up with a chat to find out why. For example, if a customer wants to start paying by credit card suddenly after a lengthy period of time using checks or ACH, it could just mean it wants the bonuses many card companies offer (e.g., cash back, airline miles, etc.). However, it also could mean the customer is facing a cash crunch—if so, it is of the upmost importance to ascertain just how bad and how temporary (or permanent) the liquidity problem is.

An order that's outside or larger than the norm or a rush order from an unknown company. Check with the sales team to determine the nature of the order and whether it has resulted from a stocking order, a sales promotion or a critical new opportunity for your firm, or if it may represent an unacceptably risky transaction.

Orders for products not typically purchased by the customer. This could indicate the customer, heading toward bankruptcy, is trying to stock up on sellable merchandise to finance its early days after a bankruptcy filing. The obvious question that needs to be asked is: “Why?” By working closely with customer service and sales, this can be the frontline in a means to prevent risky sales that may never be paid.

A sudden change in top management or ownership. Whether the company is privately or publicly held, credit managers need to conduct historical research, including a review of financial information and comparison of industry standards and credit payment history. You’ll then be able to better determine how to respond and whether to extend credit on a more solid footing.