Long Island BusinessNEWS

Survival of the suspicious

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Published: March 3, 2010
Tags: Accountancy, business, Financial Services, financial statements

In the new and unimproved world, most companies are doing worse than they were two years ago. It's crucial to take extra steps to protect your company from those sinking clients and suppliers that would drag you down with them.

"What were considered to be safe and accepted practices in the past no longer apply," said Mark L. Meinberg, managing partner for Feldman, Meinberg & Co., a Syosset accounting firm. "You have to be more vigilant about verifying customers' ability to pay and having contingency plans in place in case a major client or supplier goes out of business."

Warning signs

Last month, the Long Island Chapter of the Institute of Management Accountants featured a well-attended panel discussion entitled "Protecting Yourself from Financially Distressed Companies."

According to Neil Seiden, a board member of the organization who acted as moderator, companies must keep their eyes open for warning signs of foundering businesses.

First and foremost, be wary of changes in how you're being paid. "If a client is taking much longer to make payments or if it starts cherry-picking which invoices it pays, watch out," said Seiden, who is managing director of Asset Enhancement Solutions, a Port Washington-based financial advisory/turnaround consulting firm. "Companies normally pay the oldest invoice first, but when they get into trouble, they may pay a newer invoice that's for a smaller amount." Additionally, he noted, struggling firms may start disputing bills or asking for proof of delivery as a delay mechanism.

Another common sign of a sinking ship is the sudden resignation of a senior manager, top salesperson or a member of the board of directors, Seiden said. Be suspicious of any change in how a company does business. For instance, if you're suddenly asked to take over payments for freight delivery, it could be that the company had its credit yanked by its shipping company.

Troubled companies may liquidate equipment or a segment of their business to raise capital. They may also get dumped by their commercial bank and start dealing with a lower-tier, higher-rate lender. "A bank might demand that a company in distress hire a turnaround firm or restructuring officer," said Gerard R. Luckman, the partner who chairs the corporate restructuring group for Silverman Acampora in Jericho. As a supplier, you may get wind of this if the turnaround professional calls you to renegotiate terms. Or, you may call to follow up on a bill and find you have to deal with someone new.

A sudden large order from a client you have been pursuing might be cause for celebration. Or not. "It could be that one of your competitors cut off the company's credit," Seiden said.

Proactive research

Even if warning signs aren't visible, dig deeper. Whether dealing with new clients or long-standing ones, don't be shy about requesting financial statements, said Lee Ferber, the partner-in-charge of the business advisory group and a senior member of the health care group in the Woodbury office of the accounting firm Gettry Marcus Stern & Lehrer.

"For statements to have any credibility, they should be audited or reviewed, not merely compiled," Ferber said, noting that the latter does not reflect significant review by an independent accounting firm. Further, he said, investigate the quality of the accounting firm behind the statement.
Hire a credit reporting service and check references. "The best reference is the lender that is providing financing to the company," Ferber said. "If a company does not permit you to speak to its lender, it could be a sign of financial trouble."

Study industry trends. "If the company in question is in retail or automotive supply, there's a good chance it's not doing well," said Larry Waldman, the partner in charge of commercial audit practice development at Holtz Rubenstein Reminick in Melville.

Take steps to protect yourself

In today's world, businesses need more assurances they will be paid, and in some cases, it's necessary to demand payment before goods and services are delivered. "Consider accepting a credit card, even if you have to give 2 to 3 percent to the credit card company," Ferber said. "In questionable cases, it's better to have the payment up-front."

If you're looking to take on a major new client, consider purchasing credit insurance for your dealings with that customer. "It's an expense, but it may be worth it," Ferber said.

Letter of credit financing is coming back into vogue for international transactions. Though, like credit insurance, they add expense, letters of credit – legally binding agreements between financial institutions representing suppliers and customers – protect companies from being stiffed by overseas customers. "Over the years, when the economy was strong, companies were shipping goods on open terms," Ferber said. "Now it's going back the other way."

If a customer really wants your product, it may be willing to put up security, such as a brokerage account or a personal guarantee.

According to Seiden, it's a good idea to learn your clients' check-cutting cycles. "If they usually cut checks on the 15th of the month, call on the 10th to make sure there's a payment scheduled for you," he said. "Often, the loudest supplier gets paid."

Just as your clients are less of a sure thing in today's world, so are your suppliers. "As an accountant, I am very concerned if a client only has one major client or one major supplier," Meinberg said.

To ensure business continuity in case a key vendor goes under or gets sold to another company, your purchasing agents should be cultivating relationships with other suppliers. "If you buy $1 million worth of product from a vendor, try giving $50,000 of the business to another vender to get to know its capabilities," Waldman advised.

Working with distressed companies

So, you find out a long-standing client is just holding its head above water. Now what?

“You can’t take a book off the shelf and turn to page 25 for the answer,” Meinberg said. “You have to know your customer or vendor and make a business decision about how much credit or time to give it.”

Seiden suggests rating your clients as A, B or C in terms of health and payment history. “Limit your total exposure and how much credit you give to B and C clients,” he said.

When accounts are overdue, be proactive in working out reasonable payment plans and getting commitments from customers. And before renegotiating terms of contracts and payments, consult your attorney regarding your rights. As Luckman noted, by taking certain steps, you can elevate your position relative to other unsecured creditors in the event that the customer files for bankruptcy.