Cost Effectiveness of Disputed Deductions

BY MICHELLE DAVY, FCI

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Volume rebates, co-op advertising, defective allowances, new store openings and renovations, early payment discounts, shortages, non-compliance, portion of loss due to currency fluctuation…? And I thought I'd heard it all! It seems more and more majors have adopted these practices over recent years. There is nothing more frustrating to a credit manager than to discover they haven't received a payment due to creative efforts of placing the account payable in a negative balance, thus the supplier is shown on the statement as owing the client.

Rebates: While most major accounts streamline agreements to include volume rebates, co-op advertising and other percentages. Suppliers are often at the mercy of contractual post audit firms hired to find deductions that have not yet been deducted, but somehow after verification have been taken from payment or invoice. Should you ignore the post audit notification before the due date? If so, the client then deducts the amount from their payment.

Claims: Concealed shortages, damaged goods, pricing errors, late delivery fees and non-compliance fall into a separate category of their own. These disputed items occur on an ongoing basis and are simply part and parcel to doing business with a large customer. The cost of doing business as some have said to me over the years while I argued and fought for small amounts. While I agree that there is a cost related to keeping a client satisfied, the account running smoothly, unjust claims and rebates will rape the supplier of profits to which they are entitled when no one is paying attention. While some companies head off the bleeding by hiring personnel for the sole purpose of attacking these claims, others opt out preferring the credit note method.

The challenge: So, what is the short staffed credit manager to do?

Rebates: If tracking deductions haven't been a priority, an internal audit can be performed. When a company issues a credit note, the appropriate general ledger (G/L) accounts should be used for tracking purposes. At minimum an annual review should be instigated to verify totals attributed to each appropriate G/L and verified against total sales to individual clients for which you have contracts. The frequency should be dictated by the number of times these deductions are taken by the client. At the end of the exercise compare the amounts taken with amounts that are allowable.

Claims: Track short shipments, price differences and various other claims made by the same clients that were or were not credit noted (you may find that some perpetuate this type of claim more than others). You may in fact, discover a pattern. Are these claims disputable? What difficulties do you encounter in resolving these types of issues? The client may well be right in claiming multiple shortages and there may be an internal theft problem, so investigations of these types should remain unbiased until conclusive evidence if found.

How cost effective is this process?

Example: You have a shipment to a large client worth $71,235.89 (tax in), the client pays you $55,302.73 the disputed balance is worth $15,933.16. If operating profits are at 10%, this deduction when left untreated has already consumed more than twice the profit anticipated for the order. On the balance sheet: Your firm has sales worth $17 million annually. Budgeted discounts and allowances are worth $500,000 but a couple of large clients are taking a deduction from invoice and again from payment then a third time from post audits therefore increasing the total deductions to $750,000, say operating profits are 14% equaling $2,380,000 annually, the quarter million dollar over-deduction has eroded 10.5% of the companies total profits.

The Bottom Line

As indicated in these simplified examples, there is a correlation to unearned discounts and the company's bottom line which conversely are advantageous to the major retailer. It is no wonder that this trend in deductions and disputes has been on the increase over the last 10 to 15 years. The overall analysis is left within the boundaries of each credit department to eventually come to their respective conclusions: Is it worth the time, money and effort to:

a) fight the deductions
b) hire personnel
c) continue to sell the client or
d) ignore a potential source of lost revenues? **NCN**

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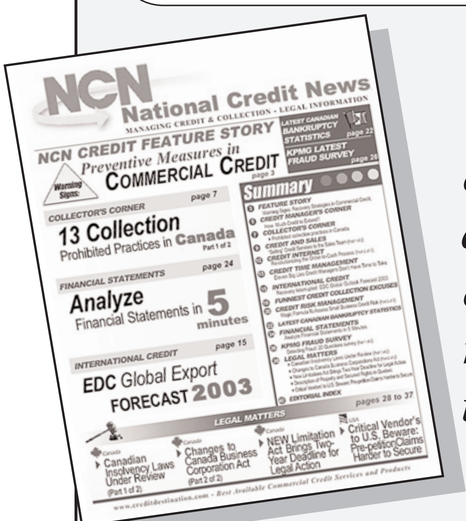

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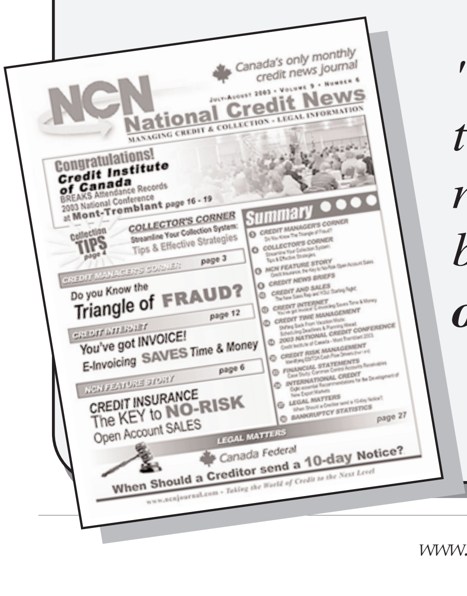

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