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# A Study on Debtors Management

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**Abstract- Debtors are people or businesses who owe you money. Proper management of your debtors will help you get paid faster and prevent bad debts. Prompt collection of debtors' accounts will also help you maintain a healthy cash flow. Giving your customer an invoice or bill after they have supplied a product or service is a way of offering credit, since you have to wait for the payment. By giving your customers time to pay for goods or services already delivered, you are making it easier for them to make purchases. This will increase sales, but will reduce the cash flow critical to your business.**

**Keywords- Managing debtors, payment terms, credit checks, credit policy**

## I. INTRODUCTION

Debt management also involves keeping debtor records - this is a legal tax requirement. There are also laws governing how you are allowed to follow up debts with your customers. Debtor management is central to the effective cash flow of your business. Without an effective debtor control system, you leave your finances vulnerable. Small-to-medium enterprises are often guilty of failing to establish an appropriate debtor management system. Even if a company simply started with tallying debtor days, it's an important first step in the right direction and a key performance indicator that, ideally, businesses should monitor monthly[1].

Managing debtors is often referred to as credit management, and includes:

- Collecting debts on time
- Setting credit limits and payment terms
- Making credit applications and credit checks
- Enforcing a clear credit policy
- Considering debtor finance.

The following guidelines will also help to establish an effective debt management system:

- Ensure all payment arrangements with debtors are always confirmed in writing
- For overdue payments, contact the debtor promptly to confirm they received their invoice
- Create a monthly debtors aged analysis
- Make sure your invoices meet your customers' format requirements
- Create a debtors day outstanding chart to identify potential cash flow improvements if your business could minimize overdue payments

Debtor management is at the heart of all businesses. Making a sale is fine, but collecting the cash is ultimately what matters[2]. After all, it is cash that pays the bills, not profit. An efficient debtor management process results in enhanced operating efficiencies, effective billing procedures and quick dispute resolution. It additionally requires less management time to be spent on administration and processing issues allowing senior management to focus on key strategic issues and on growing the business. The starting point for effective credit control is to ensure that a credit policy, including establishing normal terms of trade, is set and adhered to unless specific circumstances warrant exceptions to be made. The policy should be written down and circulated to all sales and finance staff. The process for authorising exceptions to the policy should be clearly set out and understood by all involved in the process.

Effective debtor management addresses the whole of the order-to-receipt cycle of the business from customer acquisition to order and fulfilment, invoicing, collection and dispute management. We examine below each step in the process and give ideas on ways to reduce investment in debtors.

## II. MAIN ELEMENTS OR DIMENSIONS OF DEBTORS MANAGEMENT

For effective debtor management, following elements should be analyzed

**1. Credit policy**

Credit policy effects debtor management because it guides management about how to control debtors and how to make balance between liberal and strict credit. If company does not restrict to sell the products on credit after a given limit of sale[3]. This liberated credit policy will increase the amount of sale and profitability. But risk will also increase with increasing of sale.

If we sell the good to those debtors whose capability to pay is not good, then it is possible that some amount will become bad debts. Company can increase the time limit for paying by such debtors. On the other hand, if company's credit policy is strict, then it will increase liquidity and security, but decrease the profitability. So, finance manager should make credit policy at optimum level where profitability and liquidity will be equal. We can show it graphically.

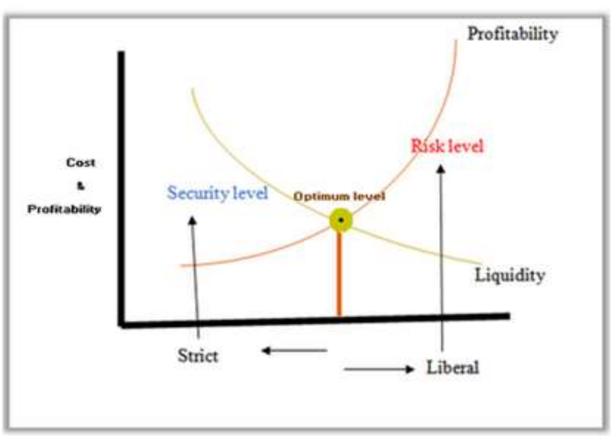


Figure 1: graph related profitability

**Sub Part of Credit Policy**

**Length of Credit Period**

Length of credit period is also an element that affects decisions of finance manager relating to manage debtors. It is the time which allows to debtor to pay his debt for purchasing goods on credit from vendor. Finance manager can increase the length of credit period according to reputation of customers[4].

**Cash Discount**

Cash discount is technique to get money fastly from debtors. It is cost of investment in credit sale.

**2. Credit Policy Analysis**

It means decision relating to analysis of credit policy. Evaluation and analysis of credit policy is based on following factors.

**Collection of Debtor's Information**

For analysis the financial position of debtors, we have to collect the information relating to debtors. This information can be obtained from customer's financial statements of previous years, bank reports, and information given by credit rating agencies. These information will be useful for deciding where debtors will our debt or not. It will also be useful for knowing capability to pay the debt.

**Credit Decisions**

After collection and analysis the debtor's information, manager has to decide whether company should facilitate to sell goods on credit or not. If company sells the goods on credit to particular debtor, then at what level it will be sold after seeing his position. For this manager can fix the standard for providing goods on credit. If a particular debtor is below than given standard, then he should not accept his proposal of buying goods on credit.

**3. Formulation Collection Policy**

For getting fund fatly from debtor, the following steps will be taken under formulation of collection policy.

- Send reminding letter for paying debt
- Take the help of debt collection agency for getting bad debt.

- To do legal action against bad debtors.
- To request personally to debtor to pay his dues on mobile or email.
- Finance manager should monitor collection position through average collection period from past sundry debtor and their turnover ratio[5].
- To make ageing schedule. Sample of ageing schedule is given below.

Good risk management at a strategic level helps protect an organization's reputation, safeguard against financial loss, minimize disruption to services and increase the likelihood of achieving business objectives successfully.

This also gives assurance on how an organization's business is managed and at the same time will satisfy any compliance requirements of the organization, where an internal control mechanism is established. Internal control includes:

- The establishment of clear business objectives, standards, processes and procedures
- Clear definition of responsibilities
- Measurement of inputs, outputs and performance outcomes in relation to objectives
- Performance Management
- Financial controls over expenditure and budget.

**4. Risk Defined**

**Risk:** is the actual exposure of something of human value to a hazard and is often regarded as the product of probability and loss

**Risk Assessment:** The evaluation of a risk to determine its significance, either quantitatively or qualitatively.

**Risk Management:** Determines the levels at which risk acceptability is set and methods of risk reduction are evaluated and applied.

**Resilience:** The ability at every relevant level to detect, prevent and, if necessary handle disruptive challenges. Source: CCS Resilience

**Business Continuity:** A proactive process which identifies the key functions of an organization and the likely threats to those functions; from this information plans and procedures which ensure that key functions can continue, whatever the circumstances, can be developed.

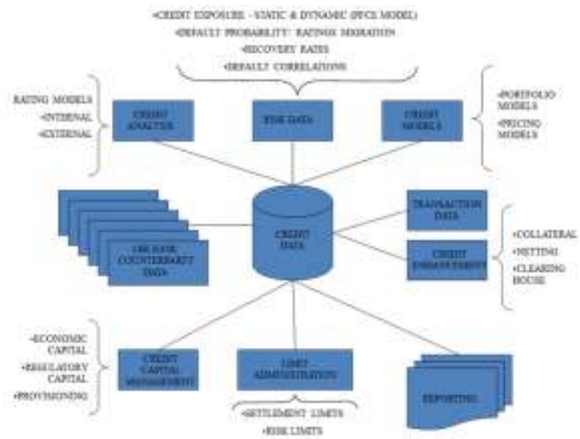

Figure 2: block diagram of credit data

## III. CONTROL ON CREDIT MANAGEMENT

The investment in accounts should be within accepted level. To achieve this, control measures are needed so that when actual fall outside the prescribed range, Corrective actions can be taken. In controlling accounts receivables certain techniques are adopted. Three such techniques are described below.

These are Debtor's turnover ratio (DTR) Debtors turnover ratio refers to ratio of sales to accounts receivable (sundry debtors plus bills receivables). The accounts receivables may be closing figure, or average of year beginning and year-end figures or average of monthly opening and closing figures. An acceptable range for the ratio is within this band, is all right.

If the actual DTR is less than 5,it means more money is locked up in accounts receivables. Either sale have slumped relative to size of debtors, or debtors have risen to sales. If the ratio exceeds the upper hand, it means customers promptly pay willingly or buy over force. It is good[6].

## IV. RESEARCH ON CREDIT MANAGEMENT

The objectives of research non credit management could be:

- To study the credit policies adopted across firms/ industries or in a firm/ industry.
- To study the extent of impact of lenient and stringent credit policies on sales, capital cost, profit, bad debts, etc.
- To study the influence of different factors like – credit allowed by suppliers, credit allowed by companies, etc. on credit policy.

### 1. Credit Analysis

It is the method by which one calculates the creditworthiness of a business or organization. The audited financial statements of a large company might be analyzed when it issues or has issued bonds. Or, a bank may analyze the financial statements of a small business before making or renewing a commercial loan. The term refers to either case, whether the business is large or small. Credit analysis involves a wide variety of financial analysis techniques, including ratio and trend analysis as well as the creation of projections and a detailed analysis of cash flows.

Credit analysis also includes an examination of collateral and other sources of repayment as well as credit history and management ability[7]. Before approving a commercial loan, a bank will look at all of these factors with the primary emphasis being the cash flow of the borrower. A typical measurement of repayment ability is the debt service coverage ratio. A credit analyst at a bank will measure the cash generated by a business (before interest expense and excluding Depreciation and any other non-cash or extraordinary expenses). The debt service coverage ratio divides this cash flow amount by the debt service (both principal and interest payments on all loans) that will be required to be met. Bankers like to see debt service coverage of at least 120 percent. In other words, the debt service coverage ratio should be 1.2 or higher to show that an extra cushion exists and that the business can afford its debt requirements.

### 2. Credit Control

Policies aimed at serving the dual purpose of (1) increasing sales revenue by extending credit to customers who are deemed a good credit risk, and (2) minimizing risk of loss from bad debts by restricting or denying credit to customers who are not a good credit risk. Effectiveness of credit control lies in procedures employed for judging a prospect's creditworthiness, rather than in procedures used in extracting the owed money. Also called credit management. People have become increasingly dependent on credit. Therefore, it's crucial that you understand personal credit reports and your credit rating (or score). Here we'll explore what a credit score is, how it is determined, why it is important and, finally, some tips to acquire and maintain good credit[8]. The financial crisis means that businesses must take control of their debtors to ensure they don’t end up in difficulties.

**The Following Three Steps Should be Implemented to Exercise Appropriate Controls Over Debtors**

**Set up Credit Controls**

Encourage customers to make payments directly to your bank account.

Use references and reports to check credit ratings for new customers, particularly those placing big orders from the outset. Such checks should identify customers that have had bad credit records in the past, so that they can be declined or closely monitored.

Set terms of trade and stick to them. It’s much easier to follow up on slow payers if your trading conditions have been clearly laid out from the beginning. Rank debtors by value and risk, and monitor accounts accordingly.

**Manage Debtors**

Deal direct with decision-makers at the customer. Monitor collections and follow up immediately if payment schedules are not met. Automatically send 30-, 60-, and 90-day reminder letters. Insist on your trade terms being met. Visit them if payments are not made on time and don't leave the premises without their commitment. Don't rely on one visit. Maintain follow up if necessary, including regular telephone reminders.

Don't finish the call without obtaining a firm commitment to make a payment. Follow up again if it is not paid on the promised date, or better still, arrange to pick up the cheque. Review credit ratings regularly for any changes in buying habits and increasing levels of debt. Long-standing customers can be the greatest credit risk, because no one thinks to check on them.

**Problem Customers**

Look out for warning signs that customers are experiencing difficulties. Sometimes they are not easy to recognise.

For instance, while the sales team may want to claim credit for any increase in a customer's ordering, the new business the customer is giving you may be the result of other suppliers removing credit facilities. Industry gossip about a company's financial position is often surprisingly accurate.

## V. CREDIT POLICY

What kinds of terms should I offer? Standard terms are usually payment within 7, 14, or 30 days after the invoice date. Don't be afraid to set your own terms, such as 50% deposit upfront or COD. Other ideas might be discounts for payment upfront, pay on invoice date etc.

The longer the term gives more reasons for invoices to go missing or be forgotten. Shorten your trading terms. Remember also to include your payment terms when quoting or attempting to make a sale. The more you mention this point, the more likely you will be paid on time.

**Objectives of the Study**

- To analysis the Debtor's management of UltraTech Cement Limited
- To find out debtor turnover ratio and average collection period.
- To find out whether it is profitable to extend credit period or reduce credit period
- To study the position of business affecting by credit risk/debtors management.
- To analysis the important financial aspect of managing the business.

## VI. DATA ANALYSIS & INTERPRETATION

**1. Data Analysis**

The calculations using in Data analysis are –

- DTR ( Debtor's turnover ratio )
- ACP ( Average collection period )
- Calculation of DTR :-

This measures a relationship between debtor's and sales.

$$\text{DTR (Crs)} = \frac{\text{credit sales (or) sales}}{\text{Debtors}}$$

Calculation for: 2023:-

$$\text{DTR} = \frac{20194.94}{1017.24} = 19.83$$

Calculation for: 2022:-

$$\text{DTR} = \frac{18270.69}{765.96} = 23.85$$

Calculation for: 2021:-

$$\text{DTR} = \frac{13205.64}{602.29} = 21.92$$

Calculation for: 2020:-

$$\text{DTR} = \frac{7042.82}{215.83} = 32.63$$

Calculation for: 2019:-

$$\text{DTR} = \frac{6385.50}{186.18} = 34.29$$

216.61

DTR from 2019 to 2023 are

Table 1: year wise DTR value

| Year | DTR |
|---|---|
| 2022-2023 | 34.29 |
| 2021-2022 | 32.63 |
| 2020-2021 | 21.92 |
| 2019-2020 | 23.85 |
| 2018-2019 | 19.83 |

DTR from 2019 to 2023 graph

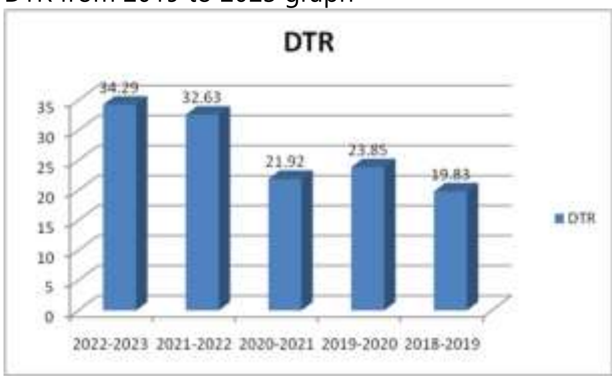


Figure 1:year wise DTR value

**Interpretation**

The Debtors turnover ratio of Ultratech cements is in the fluctuation stage because the increase and decreased in debtors to the total sales. In the current year i.e. 2023 the ratio is 19.83.

**Calculation of ACP**

The ACP calculation is compared with the firm's stated credit period to judge

The collection efficiency. The ACP measures the quantity of receivables.

Since, it indicates the speed of their collect ability.

$$\text{ACP (Crs)} = \frac{\text{Debtors}}{\text{Credit sales}} \times 360 \quad \text{(or)} \quad \frac{360}{\text{DTR}}$$

Calculation for: 2023:-

$$\text{ACP} = \frac{360}{19.83} = 18.15$$

Calculation for: 2022:-

$$\text{ACP} = \frac{360}{23.85} = 15.09$$

Calculation for: 2021

$$\text{ACP} = \frac{360}{21.92} = 16.41$$

Calculation for: 2020:-

$$\text{ACP} = \frac{360}{32.63} = 11.03$$

Calculation for: 2019:-

$$\text{ACP} = \frac{360}{34.29} = 10.49$$

## VII. CONCLUSION

Although a relatively young discipline, credit risk management has matured rapidly. Improved risk measurement and reporting techniques paired with comprehensive credit risk policies can provide extremely effective protection against credit risk losses. The best risk management techniques are operational and legal, with collateral providing the best financial risk mitigation. Credit insurance and credit default swaps offer financial protection against default, but each at its own cost—which must be compared to the benefits of reducing the specific risk it is intended to mitigate.

In view of these limitations, we believe that an alternative approach is now needed which should have two components. First we believe that the regulatory capital regime should seek directly to assess the extent to which a firm's earnings are vulnerable to stress losses of any type - a measure we refer to as regulatory equity at risk - and should then establish a capital requirement which is sufficient to provide a high level of assurance that the firm could survive such a stress event and still remain solvent during a workout period. Secondly we argue that there needs to be much more explicit regulatory oversight of the liquidity management arrangements in place at the firm, since effective liquidity management arrangements rather than capital provide the primary protection against any stress events affecting the firm

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