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MANAGEMENT OF RECEIVABLES
IN CZECH COMPANIES

Summary: The management of receivables is an important component of corporate governance, but there is only little knowledge of the way small and medium-sized enterprises manage receivables in real practice: which system, methods, and forms they use for the management and the collection of receivables, how they secure their receivables. The research among the Czech companies carried out at the University of Finance and Administration in Prague brings some interesting findings. The main weaknesses are found in the selection and identification of solvency of business partners, the insufficient or none security of receivables, the insufficient co-operation with collecting agencies, or declining legal proceeding at debt collection. The results of this research are presented in the present article.

Keywords: receivables, management of receivables, debt collection, solvency.

1. Introduction

The present period of financial and economic recession which hit, to various extent, mostly economic entities has attracted attention to the quality management of a company as a whole and also of its individual parts. The area of management of receivables has been proven as one of the important preconditions for the success of a company in worse conditions due to the reduced demand for products and services, the lack of available funds, and other phenomena accompanying a recession. As a result of the insufficiently treated system of the relationships with customers, some companies have got into secondary insolvency and other problems, resulting in adjudging insolvency proceedings. This phenomenon is documented, among other things, by the development of the number of insolvency actions in recent years (see Table 1).

This trend, however, continues because according to the data of Credit reform company, only in January 2011, further 1439 insolvency actions were submitted, from that 429 legal entities and 1010 individuals.

A good management of receivables does not mean the management of receivables only in the situation of late payment or the default to pay. It means creating the whole system of commercial relationships management so as to prevent maximally the risk of late or default payments together with optimizing the costs for this area of

Table 1. The development of the number of insolvency actions in the CR in 2008-2010

	2008	2009	Index 09/08 (%)	2010	Index 10/09 (%)
Total number of insolvency actions	5354	9492	177	16118	169
From that: legal entities	3418	5255	154	5559	106
From that: individuals	1936	4237	219	10559	249

Source: http://www.creditreform.cz/archiv (date of acces: 12.03.2011).

management and, on the other hand, to facilitate the ability to pay own payables in time. The ability to pay own payables is, as a rule, influenced by more facts (e.g. reduced demand on the market, increased prices). In spite of that fact, it is possible to consider the development of secondary insolvency in recent years to be namely the result of late or default payment of receivables by debtors; therefore, of the insufficient attention paid to the management of receivables. The solution obviously does not mean that a company will not have any funds bound in receivables – the absence of offered commercial credits would probably reduce its competitiveness.

The whole system of receivables management should be directed to the timely payment of as large part of receivables as possible and keeping the costs related with receivables management (i.e. thecosts of prevention, monitoring and collecting receivables) to the minimum. When a business underestimates these issues, even outside recession, it would be a matter of survival for that business. When secondary inability to pay occurs, a company is only a small step to insolvency and the related consequences leading up to bankruptcy or court settlement. At the beginning of 2011, the amount of debts between entrepreneurs in the Czech Republic is estimated – as stated by the periodical Lobby 3-4 /2011 – to be 1.5 billion CZK, while the total amount of past due receivables is higher than 500 billion CZK. It is obvious that these are the consequences of the economic development in several recent years, still the mentioned numbers show how important the issue is.

The recent crisis and the subsequent recession have therefore shown entrepreneurs a need for changing their attitude, among other things, to the issue of receivables and the stressed importance of their management. However, it has also referred to some shortcomings in the legislation of business relations, limiting the enforcement of law by creditors or making it difficult and costly. The most affected sector is SME, which is characteristic of firms operating in very heterogeneous conditions given by the subject of business, size, repeated supplies. This is reflected not only into higher sensitivity to changes in the economic environment, limited availability of additional sources and therefore higher dependence on timely payment for delivered supplies, but also into the form and structure of all managerial activities, therefore also in the management of receivables.

In the Czech specialized literature, a number of publications deal with the issue of the management of receivables, treating it at the theoretical as well as practical

level. The area of the management of receivables, the management of commercial credits and receivables is covered by Režňáková *et al.* [2010], Pilátová, Richter [2009], Drbohlav, Pohl [2004], Kislingerová *et al.* [2007], Vozňáková [2004], Bařinová, Vozňáková [2007], Kovaříková, Vondráková *et al.* [2003]. The related issue of payment discipline of firms is covered for example by Klimeš [2010] and bankruptcy proceedings for example by Bařinová *et al.* [2006]. Still, little is known about the way in which small and medium firms in particular manage their receivables, what system, methods, and forms they use in the management and collecting of receivables, how they secure their receivables and with whom they co-operate, and what real experience they have in this field.

The Department of Corporate Economy of the University of Finance and Administration in Prague has focused on the issue of the management of receivables namely in small and medium firms (SME) in the research project No. 7725 Management of Receivables, treated within the local grant agency. The research is carried out with the purpose of identifying the real status of the system of the receivables management in SMEs conditions. In particular, the goal is to find out how much attention firms pay to this part of management, what tools and procedures they use, what methods and procedures result in the best effects in specific conditions, what methods they use for collecting of receivables and how successful they are. The research project is divided into three stages:

1st stage: the analysis of the system of the receivables management in selected firms (case studies) – examples from practice – already completed and published [Souček 2011], the research continues in the form of elaborated dissertations;

2nd stage: the questionnaire survey focused on the identification of the status of the receivables management in SME (implemented with support for SME Association, University Hr. Králové, 1.VOX, Prague);

3rd stage: the analysis of results of preceding stages, defining the present status and the conditions of receivables management in firms (including the tax issues of unpaid receivables and the analysis of accounting impacts of receivables).

The results of the first two stages were very interesting both regarding the method of receivables management and regarding experience with their collection and success of individual methods – the results were presented at conferences and published in specialized periodicals [see for example Souček 2010, Souček, Kubíčková 2011a, Souček, Kubíčková 2011b]. Continuing the research, we have decided to perform the second part of the survey at the second stage which would complete and correct the findings achieved in the first survey. The results of the verification are included in this article.

2. Methods of the research

In the second part of the questionnaire survey, we used the same questionnaire as in the first part. The respondents were mostly the students of the combined studies at

the University of Finance and Administration, with the specialisation in corporate management and corporate finance, focused on SME. The composition of the sample of respondents as to location and subject of business, legal form, as well as size were similar to the first sample of respondents. For the specification and classification of SME, the criteria were used again as accepted by the European Union with validity from 1 January 2005. A small and medium-sized enterprise is defined according to three main criteria: staff number, yearly turnover in million EUR, and the value of assets sum in million EUR. All three SME categories were represented in a relatively equal proportion in the new sample. As to the region where they operate, firms operating in the capital and in small cities were in the same proportion, a smaller part operated in a regional capital. As to the subject of business, trade firms were mostly represented, approximately one quarter of them was production firms, the rest were firms dealing with production, trade, as well as the provision of services. What was newly represented was the firms partly funded from the state budget although in a small proportion.

3. Achieved results

3.1. The results in the field of receivables management and the prevention of unpaid receivables

The results of the second survey of the research confirmed that considerable attention in firms is paid to the field of receivables management and the prevention of unpaid receivables although not always adequate methods and procedures are used.

In the second sample, the credibility of customers is largely checked prior to the conclusion of commercial contract – in 70% firms. However, there are still 30% of the firms which do not pay attention to customers and their ability to pay. In most of them, i.e. 57% of the firms, therefore in a smaller part, a new contract and payment conditions are defined basing on past experience with customers. The utilization of the limits of supplies/commercial credit was not, however, discovered in such a scope – only 30% of the firms stated their utilization, while the remaining 70% of the firms do not use supplies limits. Also discounts or other benefits frequently used abroad for customers motivation to pay their payables in time were identified in this part of research as neglected – using a discount was identified even less frequently, only in 20% of the cases, while almost 80% of the firms do not use that tool. This confirmed the fact that in the CR, this tool for receivables management has not yet found its place. On the other hand, 27% of the firms reported that they use also other tools for the motivation of customers to pay in time, which allows us to assume that attention is paid to this area. Nevertheless, more than one half of companies do not deal with this area. These results are presented in Figure 1.
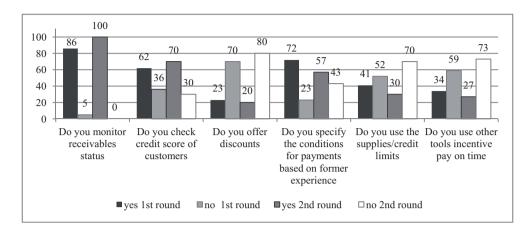
Fig. 1. The management of receivables in prevention of unpaid receivables

Source: authors' own study.

3.2. The results in the field of continuous monitoring of receivables

In the field of the continuous monitoring of receivables, also the second part of survey discovered that the firms which do not pay much attention to receivables during their life act only in response to the failure to pay them in time with reminders and other tools. On the other hand, most firms monitor receivables and their development. However, regarding the method and intensity of monitoring, procedures again differ strongly: from regular monitoring in intervals from 1 to 3 up to checking maturity once a month, based on accounting data or by random check in the case of a problem.
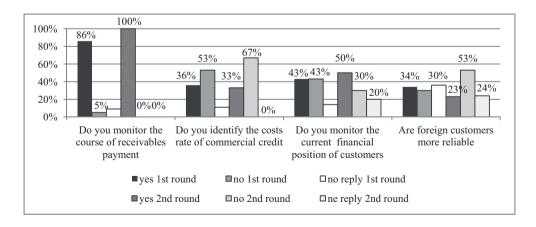

Fig. 2. Continuous monitoring of receivables

Source: authors' own study.

The method for monitoring is mostly linked to accounting records and the records of invoices maturity within them. A more detailed analysis discovered a relation with the firm size. Bigger firms pay more attention to the issue, smaller firms probably do not have enough time, sources, and personnel.

The evaluation of the conditions of commercial credit using more analytic methods is used to a small extent also in this survey. Seventy percent of the firms do not assess the costs of commercial credit. The link is again strong between this activity and foreign trade contacts of firms – almost all the firms with customers abroad reported that they assess the rate of the costs of commercial credit. One half of the responding firms deal with continuous monitoring of financial situation of clients.

3.3. The results in the field of solution of unpaid receivables

Seventy seven percent of the firms confirmed experience with the enforcement of a receivable, which is by 8% less than in the first survey. Also here, it is possible to derive from these answers the link between the fact that firms which have to deal with the collection of receivables at the same time reported that they do monitor neither the status of their receivables, nor the situation of customers, do not use tools motivating customers to pay in time or limits for supplies according to experience with the payment discipline of clients. This fact confirms that more attention paid to receivables influences the reduction of problems with their payment.

Again, receivables were most frequently collected using remainders (67% of the firms), but often reminders were accompanied with other procedures, like the negotiation with a debtor (22%) or the limitation of further supplies (47%). Besides, the proportion of the collection of receivables using agencies or through a court action was discovered to be relatively small (only 10% of firms), which is less by more than one half than in the first survey (27%), and the sale of receivables is used by 3% of the firms, which experienced a relatively strong decrease against the findings of the first survey (27%). The responding firms confirmed that the most successful forms of receivables collection are the negotiation with a customer (53%) and the limiting of supplies (27%), while the smallest effectiveness is again linked with the sale of receivables (3%) and the enforcement using an agency (3%). A slightly higher success is attributed to a law office (20% from the original 16%). Among the firms co-operating with law offices, more than 90% assess the co-operation as successful, which means an increase, comparing to the first survey.

The consequences of unpaid receivables were discovered most frequently in the form of the write-off of a large amount of receivables. This fact, again with a relatively large proportion of firms which had to write-off several receivables during past five years (50%) confirms that unpaid receivables entail a fundamental burden for most firms. According to the responses, the costs of receivables enforcement range within a wide interval – from tens of thousand crowns to mere postal fees and

telephone bills, which again can be considered as the reflection of firms' conditions for collecting the receivables, but also of the subject of a business, firms' size, etc.
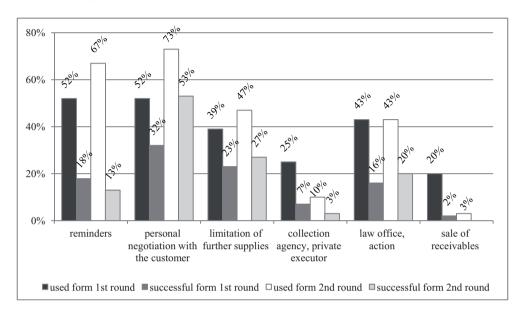

Fig. 3. Thw forms of the enforced collection of receivables and their success

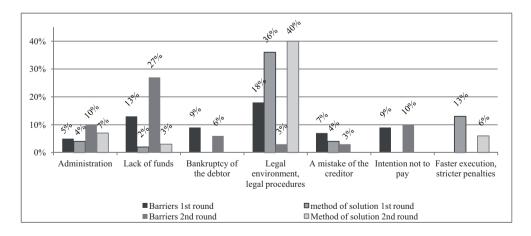Source: authors' own study.

Fig. 4. The causes of the problems with receivables collection and proposed solutions

Source: authors' own study.

In this second part of the survey, the most frequently reported cause of the problems with the enforcement of receivables was insolvency and insufficient

legislation for commercial relationships in the CR law, the insufficient enforceability of law, and the lengthy work of courts. Also here, problems are mentioned like unfair intention or a firm dissolution. This is reflected also in the opinions on methods for the solution of a situation – prevailing requirement is to improve laws and regulations, speed up work of courts and executors, and impose generally stricter recourses against debtors.

4. Summary and discussion

Based on the findings achieved in the second part of the questionnaire survey, it is possible to summarize that the findings and conclusions achieved in the first part were confirmed as to all treated issues. Most firms pay attention to receivables management at all three stages, formulate their future business policy based on the past experience rather than on the present situation in the business environment. In the smaller number of cases, they check clients and secure their receivables at least by the limiting of provided commercial credits. Less attention is paid to tools and methods purposefully focused on the timely payment of receivables – the utilization of a discount as a tool to motivate earlier payments, as well as other methods motivating to pay in time, but also other forms of securing, like bank guarantees, the insurance of commercial credits, advance payment, guarantee, retention right, contractual penalty, or penalty interest. Also here, the important fact was confirmed that the success or the low effectiveness of the enforcement of receivables is caused by unsuitable legislation and overall legal environment, influencing also the attitude and the payment discipline of debtors. Also the second part of the survey confirmed the influence of various conditions under which SMEs operate (subject of business, size, etc.). The achieved findings can therefore be used as an aggregate for more general conclusions and recommendations for SMEs.

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ZARZĄDZANIE NALEŻNOŚCIAMI W FIRMACH CZESKICH

Streszczenie: Zarządzanie należnościami jest ważnym elementem ładu korporacyjnego, lecz wiedza o sposobach, w jakich małe i średnie przedsiębiorstwa zarządzają należnościami w praktyce biznesowej jest ograniczona. Dotyczy to przede wszystkim pytań o to, jakiego systemu, metod i form używają w zarządzaniu i pobieraniu należności, a także sposobów zapewniania sobie skutecznej windykacji. Badania czeskich firm, przeprowadzone przez Uniwersytet Finansów i Administracji w Pradze, przyniosły interesujące wyniki. Główne braki stwierdzono w obszarach selekcji i identyfikacji wypłacalności kontrahentów, niedostatecznego bądź nieistniejącego zabezpieczania należności, niewystarczającej współpracy z agencjami windykacyjnymi oraz z powodu odstępowania od postępowań sądowych podczas windykacji. Wyniki badań zaprezentowano w niniejszym artykule.