collective szabo wisdom®

SZABO ASSOCIATES, INC. VOLUME 11, ISSUE 1, MARCH 31, 1996

Dear Friends:

This year is noteworthy for Szabo Associates, Inc. because it marks our 25th year in business. As we celebrate our longevity, we also celebrate our continued growth. (Our recent office expansion brings us to 10,000 sq. ft. to accommodate our growing staff.) We look forward with enthusiasm to our next quarter of a century and thank all of our friends and clients who have contributed to our success over these many years.

On our spring Szabo calendar are the National Association of Broadcasters Convention in Las Vegas, Nevada, April 15th through 18th; the Broadcast Cable Financial Management Association Convention in Orlando, Florida, May 19th through 22nd; and the Cable Advertising Bureau Convention in Atlanta, Georgia, June 23rd through 25th. See y'all then!

Best wishes for a great spring season,

Pete Szabo, President
Szabo Associates, Inc.

International Business—Part 2

Evaluating Customer and Legal Issues

In our last issue, we talked about the importance of evaluating the creditworthiness of a potential foreign customer's *country* prior to evaluating the risk associated with the individual customer. Only if the country risk is deemed acceptable should you begin evaluating *customer risk.* Additionally, always consider customer risk *in light of* country risk when determining credit terms. For example, you might choose to deny open account terms to a creditworthy customer with a high degree of country risk.

CUSTOMER RISK

Evaluating foreign customer risk involves essentially the same process as in the domestic marketplace. A sound credit decision must be based on gathering and analyzing factual and timely information (payment history, credit reports) on the customer. The process is carried out simply for the purpose of determining whether or not a foreign customer is acting in good faith and is not overestimating its ability to pay.

In both the domestic and international marketplace, credit managers should determine customer risk by carefully considering basic facts regarding what are commonly called the **"Four Cs of Credit"**: **character** (reputation for honesty and willingness to pay on time); **capacity** (ability to conduct business successfully and level of automation); **capital** (as determined, if possible, by consolidated year-end financial statements for the last three years, prepared by an outside CPA or reputable accounting firm); and **conditions** (external factors, such as hurricanes or competition, unrelated to other credit issues).

Getting credit and financial information on foreign customers can take several weeks. The sales department should inform the credit manager of a prospective foreign customer as soon as possible, even if the salesperson is doing only some preliminary investigating of potential customers in certain countries. Ample lead time not only can reduce the chance of an unwise credit decision but also can prevent the salesperson from wasting time pursuing a potential customer who is not creditworthy or whose country is considered a high risk from a credit point of view.

Sometimes the sources of information on foreign customers are limited or unreliable. In such cases, trust, logic, common sense, and good judgment—which should always be important elements in the evaluation process of any customer—assume an even greater role.

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International Business

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NAVIGATING THE LEGAL WATERS

For those of us doing business internationally, the law assumes relevance when the deal "goes south." By paying attention to legal and regulatory matters at the outset, however, you can avoid troublesome and costly problems later.

There are two types of legal issues affecting international credit management. *Private law* deals with relationships between parties to individual agreements. The rules of private law (the law of contract, for example) define the nature and consequences of business dealings and fill in the gaps in agreements. *Public law* deals with governmental regulations put in place for the public interest. Its rules direct and limit what the parties can do and how they can do it. Because these private and public laws help define rights, duties and responsibilities as well as sanctions, compensation and penalties, the credit manager should consider them valuable in evaluating risk.

Private Law Issues. All legal systems accept the principles that parties are free to agree on what constitutes the deal and that they are then obliged to perform as agreed upon. Systems vary, however, in the ways they qualify and restrict these principles. For example, a party may be disburdened of the obligation to perform by an act of *"force majeure"* (war, natural disaster, economic upheaval), which makes performance impossible.

International business and finance have developed many uniform instruments and practices that have global relevance, such as letters of credit, first demand guarantees, and syndicated loans. The legal acceptance of these instruments rely heavily on general principles of the law of contracts and obligations, and such deals are usually conducted according to widely accepted standard ground rules of the industry.

Associations representing business interests frequently draft rules and contract forms for transactions, some of which gain industry-wide acceptance internationally. Since these provisions are drawn up by private bodies with no legislative power, they bind the parties to individual deals only if the parties agree to apply them, usually by specific reference in the contract.

Still, no comprehensive transnational business law, accepted on a uniform basis throughout the world, exists. Additionally, no international business courts to hear disputes between businesses exist either. Contracts involving more than one country are usually subject to national (municipal) laws, and disputes are heard by national or local judges unless the parties agree to a private arbitration procedure.

To complicate matters further, an international contract may be governed by one of several different laws—the law of the country in which one of the parties is established, a legal system designated in the agreement, an intergovernmental convention, or a mixture of all of these—the choice of which can have a significant impact on the rights and responsibilities of the parties involved.

Each country has its own rules to determine whose law applies to an international contract if a dispute occurs and the contract does not address the problem. These are called "conflict of law rules" or "private international law." The latter is a bit of a misnomer since the legal rules used to choose the law and the law chosen are generally both national laws. Only the dispute is international. The trend is to apply the law of the country to which the agreement is most closely tied—often the place where the contract has to be carried out.

So … when the parties, who are established in at least two different countries, start arguing and cannot settle their differences, who will hear their case? This is a different issue from that of deciding whose law is applicable. A court that decides it has jurisdiction to hear an international case may apply a foreign law, and the country whose law is applicable may not be the right one in which to judge the dispute.

While the approach varies among countries, in general a court will agree to hear a dispute involving parties in different countries if it decides it has jurisdiction over the parties or the issue. The problem might be avoided altogether, however, if *in their contract* the parties agree on whose court will hear the case should a dispute occur.

An alternative to national courts is arbitration. Ordinarily this is accomplished by including a general arbitration clause in the original contract. The parties can agree to arbitration when the problem arises, but the chance for any kind of agreement at that point is diminished. Arbitration can be *ad hoc*, in which the parties directly appoint the arbitrator, decide on procedural rules and administrative procedures that are to apply to the case, and negotiate fees. The second

alternative is arbitration administered by a specialized institution with formal administrative rules. Examples are the International Chamber of Commerce Court of Arbitration, the London Court of International Arbitration, the American Arbitration Association (AAA) and the International Centre for the Settlement of Investment Disputes (ICSID) attached to the World Bank.

Arbitrators apply legal principles to make their decisions. In some cases they may lean toward accepted international business practice rather than the strict confines of a particular national system, and they tend to emphasize the obligations inherent in contractual undertakings. Generally, there is no appeals system.

Litigation proceedings may be used to recover a simple money debt in cases where there is no dispute regarding liability or amount owed. For such situations, many courts offer accelerated procedures, which are likely to be more expeditious and less costly than arbitration.

Public Law Issues. A country's views on the public interest can limit a buyer's and seller's freedom to make a deal of their choice. Examples are exchange control regulations, anti-trust rules, financial reporting requirements, and taxation law.

Insolvency is also a public law issue, and procedures can vary widely among countries. Proceedings under Chapter 11 of the U.S. bankruptcy statutes are a prime example.

Another public law issue is *sovereign immunity,* which prevents private parties from suing a foreign state without its consent and from seizing its property to satisfy an award. Courts and arbitrators increasingly rule, however, that sovereign immunity cannot be pleaded by a state party engaged in commercial activities. A state may waive immunity in contract by agreeing to submit disputes to a particular court or arbitration system. Even if a state or government agency is not granted immunity from being sued, however, it may still be able to plead that certain of its assets cannot be seized to satisfy a judgment against it. The U.S. Sovereign Immunities Act provides that assets can be seized only if they were used for commercial purposes and one of a number of alternative conditions is met.

In Summary. Every company that does business internationally should have a coherent policy for its global credit operations, and as a credit manager, you should be able to answer "yes" to the following quesions regarding that policy: Do you employ maximum use of internationally recognized rules and conditions? Do your contracts include a properly drafted arbitration clause? Have you identified all important legal and regulatory issues to be covered in the contract? Within the policy's general framework, do you allow for flexibility in application to accommodate differences among countries?

Acknowledging that the entire international trading community is based on elements of trust, goodwill, and prudent judgment, analyze carefully the information available to you regarding the customer and the customer's country. Then ask yourself the following: Is the sale worthwhile in relation to market plans, objectives, and strategy? Do the rewards outweigh the risks in extending credit to the foreign customer? Will there be any rewards if the risks are high? What is the cost/benefit of the deal?

Doing business internationally can be an exciting foray into profitable territory. Proceed carefully and enjoy the adventure! ♦

YOU KNOW THAT FOREIGN PROSPECT YOU ASKED ME TO CHECK OUT, BOSS? WELL FROM WHERE I STAND, THINGS COULDN'T LOOK BETTER!"

Why We Work the Way We Do
Our Collection Process

Clients sometimes ask us, why is it that we can get results after they've spent weeks running into a brick wall?

The answer is in the way our people have learned to work. Call it technique. Call it know-how. It works.

The truth is, most people dread talking to their customers about overdue bills. Even other collection services dread the confrontation and hassle. So what do they do? They send a form letter. In too many cases, that's a waste of paper. No matter how threatening it is, a letter is ridiculously easy to throw into a waste basket.

We use the phone call. When it comes to collections, there's no substitute for person-to-person discussion. Our people are trained and experienced in making maximum use of the telephone. We're experienced in avoiding confrontations, except on those occasions when a confrontation can deliver the payment.

That isn't easy to do. Our people have been selected for their intelligence and personality, then thoroughly trained in diplomacy and negotiation. They've been intensively trained in the media field they'll specialize in. By the time they get on the phone with your past-due client, they're ready to take control of the conversation.

Because of the way we're organized, our representatives on the phone are supported by administrators with a wealth of know-how and experience. These are people who have overcome almost every collection obstacle you can imagine. We also support our representatives with the world's most complete database on advertisers and agencies, along with a comprehensive Library Resource Center.

So when you have an overdue account that seems impossible to collect, don't give up. You may be surprised what a Szabo representative can do. ♦

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