collective szabo MEDIA COLLECTION PROFESSIONALS wisdom®

SZABO ASSOCIATES, INC. VOLUME 24, ISSUE 1, MARCH 31, 2009

Dear Friends:

While these are certainly challenging times for media, I believe that challenge creates opportunity for organizations to review policy and procedures, strengthening those that promote profitability and discarding those that don't. This issue's feature relates some true stories, straight from "the trenches" at Szabo, that illustrate just how much, for better or for worse, an organization's credit and collection practices can affect the "collectibility" of delinquent accounts.

Our spring calendar includes MFM/BCCA (Media Financial Management Association/Broadcast Cable Credit Association) and INFE (Interactive and Newsmedia Financial Executives), which are co-locating their annual meetings at the Westin Peachtree Plaza in Atlanta, Georgia on May 12-14. We'll also be attending the International Licensing Industries Merchandisers' Association, Licensing International Expo, May 31-June 4 in Las Vegas, Nevada.

Best wishes for a wonderful spring,

Robin Szabo, President
Szabo Associates, Inc.

The Good, The Bad, and the Ugly ...

Keep Receivables Collectible During Bad Economic Times

As the country's economic woes continue, credit and collection managers have been "hanging tough," trying to accommodate their organizations' sales-driven focus as well the need to collect according to their terms in order to protect profits. Not surprisingly, while organizations have intensified their sales efforts to compete in weakened local and national advertising markets, many past due accounts that in different circumstances might have been resolved in media's favor are becoming virtually uncollectible.

In recent days, Szabo has been involved in a number of accounts with seriously compromised "collectibility." While some of the circumstances that rendered these accounts difficult to collect could not have been easily predicted, many could have been prevented or at least mitigated. The following stories illustrate the "Good" (what can and should go right), the "Bad" (what can go wrong and negatively affect the outcome), and the "Ugly" (what can go terribly wrong and is rarely salvageable). All are true, with names withheld to protect the identities of the parties involved.

The Good.

An advertising agency placed buys on television, radio, and cable networks. The orders from the agency included a payment liability disclaimer. Some of the creditors obtained a credit application from the advertiser, signed by the advertiser's chief financial officer. The advertiser failed to pay the agency, and the creditors' inquiries to the advertiser received no response.

Szabo received the claims for the unpaid accounts, which ranged from 90 days to more than a year past due. Because we were able to demonstrate the advertiser's liability with the signed credit applications, we collected the "early placers" (aged 180 days or less) before the advertiser filed for bankruptcy.

This case illustrates the value of (1) determining who is responsible for payment prior to running the advertising; (2) getting written confirmation of that liability for payment; and (3) placing past due accounts for collection in a timely manner.

Our second "good" example involves an advertising agency that placed a buy with a magazine for a well-known advertiser. The magazine obtained from the agency a signed credit application, which included the magazine's joint and several liability clause, and "noticed" the advertiser by sending it a copy of the signed application by certified mail. The agency went out of business after paying the magazine for some, but not all, of the advertising.

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Upon receiving the claim, Szabo contacted the advertiser, who initially refused to pay on the basis that its contract had been solely with the agency. After presenting the credit application on the agency as evidence that the advertiser had been notified of the magazine's joint and several liability position, we were able to collect not only the amount that the advertiser had not paid the agency, but also 50% of the amount that the advertiser had paid the agency but that the agency had not paid the magazine.

This case illustrates the value of (1) getting a signed credit application; (2) including a joint and several liability clause in the credit application; and (3) notifying all parties involved in the buy, in a verifiable manner, of your joint and several liability position.

The Bad.

A large national banking institution (the advertiser) contracted with a large and well-known advertising agency, which the advertiser paid in full for a July through September schedule. In mid-September, the advertiser filed for bankruptcy. The agency, concerned that the bankruptcy court may issue a preference demand for the money it received from the advertiser, sent letters to the stations stating that (1) the stations would receive only 75% of the amount due, with the agency holding back the remaining 25%; (2) if the agency received a preference demand, the agency would be allowed to renegotiate the amount owed the stations; (3) if the demand were for an amount greater than the amount already paid to the stations, the stations would have to share the financial burden of the demand; and (4) the stations would have to pay the legal cost of the preference defense.

As is the case with most advertising agencies, this agency operates on a sequential liability basis, which obligates the agency to pay the station if the agency has been paid by the advertiser. By the agency's own stated position, it would seem clear that the stations should be fully paid; however, when faced with the possibility of having to pay the money back because it might be deemed a preference payment, the agency attempted to alter its own liability position.

Attempts by agencies to protect themselves from preference actions are nothing new. In 2006, Omnicom's OMD unit, the third largest media buyer in the world, attempted to proactively eliminate this risk by amending its sequential liability clause. The additional wording—-*"In the event Agency returns to the advertiser any such amount paid Agency by the advertiser, then Media Company will similarly repay such amount to Agency and look solely to advertiser for payment"*—was removed after meeting strong objections by media. (See *Collective Wisdom*, December 2006.)

We categorize this case as "bad" rather than "ugly" because there is a fair chance that the agency will prevail in court by showing that the advertiser's payment was made "in the ordinary course of business." (See *Collective Wisdom*, December 2004.) On the other hand, without this resolution, chances are that recovery will be difficult and partial at best. So how could the balance of risk have been shifted in media's favor?

As some agencies and buying services have been not only reactive but also proactive in their attempts to limit their liability for payment, so should media! Simply holding a position without ensuring that all parties are aware that you intend to enforce it is akin to having a guard dog that is missing all its teeth.

This case illustrates the importance of (1) recognizing the failure of the sequential liability position, which virtually all agencies hold, to allow media fair recourse in the event of nonpayment or preference actions; (2) holding a joint and several liability position and notifying all parties involved prior to running the advertising; (3) reiterating your joint and several position on every invoice and written communication; and (4) monitoring troubled industries. Although the advertiser in this case paid the agency in full, the stations incurred risk because of the advertiser's subsequent bankruptcy, exposing the stations to the risk of preference actions.

The Ugly.

The advertiser contracted with an agency for a January through March schedule and paid the agency for January and February. The agency subcontracted with a large, well-known media buying service. Prior to billing the advertiser for March, the agency went out of business. The buying service received no payment at all.

The advertiser, unaware that the agency had subcontracted with the buying service, refused to pay the stations for March because its contract was with the agency only. The stations did not want to pursue the subcontracted buying service because it is a major player in the business. Because of their strong sales-driven focus, the stations did not want to pursue payment from the advertiser either.

This case illustrates that (1) complete disclosures could

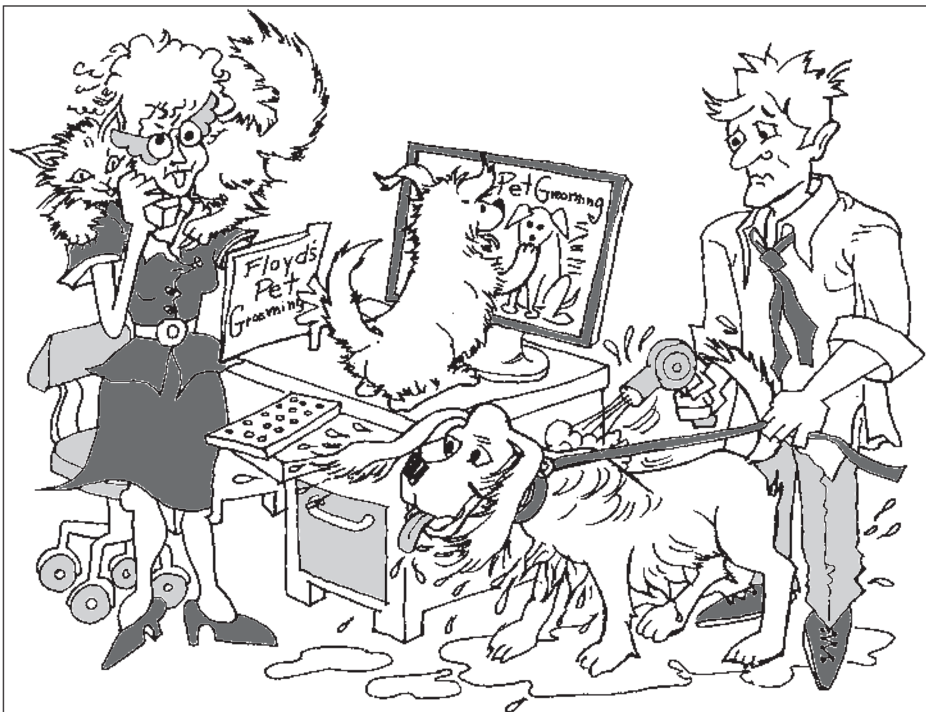
have prevented this case from becoming an "ugly" scenario in which the stations have no acceptable recourse. The stations should have asked the agency if there was to be any third party involvement in the buy; and (2) all participants—the advertiser, agency and buying service—should have received notice of the stations' joint and several liability position.

Our second "ugly" example involves a large, reputable, 50-year-old advertising agency with a roster of sizeable accounts, including its state's Lottery. The patriarch of the agency died, leaving the business in the hands of his children. The children failed to run the agency wisely, factoring their accounts receivable and pledging all assets to a bank to secure financing. The bank called the agency's note, while millions of dollars were still owed the agency by the Lottery. The Lottery wanted the money to be paid to media, which had not yet received payment; however, since the bank had perfected its security interest, the Lottery was required to pay the bank instead of the media properties.

This case illustrates (1) the risk of doing business with agencies without proper due diligence. Media had no signed credit application and no joint and several liability clause; and (2) media's failure to recognize the "red flag" raised by the agency's change in operations, although they were aware of the owner's death. Had they paid proper attention to the impact that the new managers were having on the business and enforced payment terms, the damage may have been mitigated or avoided.

Our final story is a simple one, but equally "ugly." The station had the credit application of an agency on file. The agency submitted a large order, which also included a disclaimer stating that the agency was not responsible for payment to media if the advertiser failed to pay the agency. The station's sales manager, without consulting with or notifying his business department, honored the agency's request to sign the order (and sequential liability clause) and return it to the agency. The agency refused to pay media because the advertiser failed to pay and went out of business.

This case illustrates (1) the need to consistently adhere to your organization's joint and several liability position. By signing off on the agency's sequential liability clause, the sales manager effectively eliminated any argument that could have been made regarding the agency's responsibility for payment. Even if the signed credit application on file included a joint and several liability position, the clause would have been invalidated by the sales manager's signature on the later document; and (2) the importance of cooperation and communication between departments. Had sales given credit and collections the opportunity to review the agency's document, chances are that this problem would have been avoided.



"When we said we were willing to work with you, Floyd, we were talking about a plan to pay down your past due account."

In bad economic times, prudent credit practices and disciplined collection processes are essential for maintaining profitability. When credit and collections take a back seat to the quest for sales, collection efforts often become inconsistent and getting paid becomes increasingly difficult. Here are a few tips for maintaining profitability during these uncertain times:

1. Know exactly who is responsible for payment and get signed documentation to prove it. While contracts are best, signed credit applications are a close second.

2. Include a joint and several liability clause on contracts, credit applications, invoices, and all written communications with the customer.

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Notify all parties involved in the buy of your liability position by certified mail or other verifiable means prior to running the advertising.

3. Keep the communication lines open between sales and credit. Tough times offer the temptation to become lax on enforcement of policies and procedures, and a "unified front" is critical to staying on top of receivables.

4. Monitor advertisers' industries, even if your contract is with a strong advertising agency. Agencies' sequential liability position poses risk for media if troubled advertisers fail to pay them, and an advertiser's bankruptcy can expose your organization to the consequences of preference demands.

5. Keep your receivables young. The point at which a customer fails to meet the terms of your contract is the point at which profit on the sale begins to deteriorate. Bill promptly and accurately. Prompt billing aids the collection effort because the sooner the invoice is sent, the sooner it enters the customer's payable cycle. Institute systematic actions that will be taken as the account ages. Actions taken during the first 90 days of the billing cycle can determine whether the bill is collected. We recommend, if your terms call for payment within 30 days, starting the collection process on day 45 with follow-up at least once a week.

6. Suspend future schedules or revoke credit privileges on 60-day past due accounts. If you choose to continue to do business with the delinquent customer, insist on cash-in-advance for new advertising, and negotiate an agreement to pay back the overdue amounts.

7. Place accounts for collection when they are between 90 and 120 days past due. The longer an account stays on the books, the more it costs to keep it there and the less likely it is to be collected at all.

Every receivable dollar is more valuable during recessionary times. Recognize that accounts are more perishable now, be certain of your procedures, and act promptly at the first sign of trouble to prevent a "good" collectible account from becoming "ugly"! ♦

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