

READING

CREDIT INVESTIGATION RESOURCES

Major in-house and external sources of commercial credit information include government agencies, reference materials, periodicals, comparative analytical tools, trade associations, public records, banks, and trade inquiries.

- **Reference materials and periodicals**—The number references for a credit investigation could fill a small library. Websites and books have been written solely to enable the reader to locate the appropriate information. Also, trade periodicals, business newspapers and magazines, and daily newspapers may supply information. Although it is unlikely that much substantive information about a small, local business will be found in a trade or national business periodical, such publications are useful in assessing national or industry-wide economic conditions and trends. On occasion, the local newspaper may print an article that refers to a current or prospective customer

In Level 2 Course 3 of this curriculum we provided some examples of industry and trade association references as shown in the box below.

Industry and Trade Association Examples

Industry and trade associations, plus governmental entities, colleges and universities, can provide industry information, plus data based on basic financial ratios, but more often cover statistics or ratios that are somewhat unique to their own industry. The following are examples:

The website for the National Association of Motorcoach Operators (www.namocoaches.org) provides unique data and statistics, such as the industry having about 4,000 companies, with 90 percent operating fewer than 25 buses. About 50 percent of the active job positions in the industry are with firms with fewer than 50 total employees. The association also tracks items such as annual revenue per bus, etc. This is information that goes far beyond current ratios and leverage ratios, and is equally important to understanding a commercial borrower.

Governmental entities, such as the U.S. Department of Agriculture, provide extensive information on crop yields and pricing. Most major commodities also have a dedicated industry group. For example, the National Cotton Council of America (www.cotton.org) provides data on production, production history and yield from the county and state level in the U.S., to worldwide data. It also provides the following technical resources that would be ideal for a business banker attempting to learn the industry:

- Bale packaging (standards, specifications, and updates)
- Biotechnology (reports and studies on biotechnology, plus links to other resources)
- Cottonseed (information on cottonseed and cottonseed products)
- Flow-shipment (warehouse reporting information, shipping standards, rack sample study and related reports)
- Pest management (information on boll weevils, cotton nematodes, and cotton seedling diseases)

Colleges and universities also can be a source of information, sometimes in cooperation with an industry group. Since 1980, the Recreational Vehicle Industry Association (RVIA) has commissioned the University of Michigan Survey Research Center to update various industry statistics every four years. The most recent study cited a 15 percent increase over the four years in numbers of RV owners, now reaching one in twelve households in the U.S.

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- **Comparative analytical tools**—Several resources help to determine how one business compares with others in its industry. The Risk Management Association (RMA) Annual Statement Studies provides composite financial statement data and key ratios for hundreds of businesses, grouped by industry classifications. Each year RMA members submit summary financial data on companies they have analyzed, in a standard format including North American Industry Classification System (NAICS) code, sales, and asset sizes. RMA sorts and provides statistical data on the financial profiles and key ratios by entire industries, then within relevant assets size ranges and revenue size ranges, as dictated by the sample sizes for each industry. More information about the RMA Annual Statement Studies and financial ratio analysis are found in Level 2 Course 3 of this curriculum
- **Public records**—Information about business transactions often is found in records at the office of the county clerk (or city/town clerk in some states, as well as probate judge in others), courthouses at the state or federal level, and in Uniform Commercial Code (UCC) filings, primarily at the state level. These records include the ownership of the business; ownership, pledge, and transfer of real and personal property; assessed valuation of real estate for tax purposes; corporate charters, and other formation papers; occupational licenses; and suits, judgments, and other judicial proceedings. Federal cases, including bankruptcy proceedings, are recorded in federal district courts. The office of the secretary in each state or the state corporation commission usually can verify the name of the business and its “good standing” existence. This verification is especially important when dealing with a new customer
- **Government agencies**—Federal and state government agencies can provide useful resource materials, including websites, books, periodicals, indexes, and census data. State departments of commerce are another good source of information. At the federal level, numerous departments, and agencies issue reports on price levels, sales, production levels, inventory, trade activity, and other key financial data for different industries. Particularly useful are federal government publications from the Government Printing Office
- **Bank checks**—One of the first steps in a credit investigation is to check as many bank records as possible. While this was an accepted practice many years ago, today, for fear of litigation over providing derogatory information, many banks will not respond to a credit check. Also, in a situation where the business banker is soliciting a business to move from its existing bank, it may not be wise to inform the existing bank of the attempt to take a customer. Even in “friendly” situations where banks are cooperating to extend credit, or the creditor is a complementary source of credit information, privacy laws govern the release of credit information

In situations where it is possible to obtain information from another bank, the following issues should be considered: First, if the business previously borrowed from the same bank, the bank should have a credit file. The borrower also may have other accounts at the bank that provide pertinent information. In larger banks, the trust and investment departments may have other account information.

Second, if a lender makes inquiries to other financial institutions, such as commercial banks, mortgage lenders, and commercial finance companies, information should be available about deposit types and balances; amounts, types, and collateral for loans outstanding; borrowing history, and payment habits; and customer character. We will discuss requesting credit information later in this module.

- **Trade checks**—Suppliers for the customer’s business should be contacted. Trade checks are particularly useful in determining the extent to which a business relies on its suppliers to finance current assets, and how those accounts payable are handled. For example, in calling several trade suppliers about a loan to finance fixed assets, a business banker may discover a disproportionately large amount of trade credit outstanding. The lender might conclude that the customer’s critical need may be for a loan to finance permanent levels of inventory, which could increase the loan amount from what was originally requested. Contacting customers of the borrower is also important to obtain information on amounts owed, anticipated future sales, and a general business reference.

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- **Personal credit history**—Finally, if the bank requests a personal guarantee, then a personal credit bureau report (CBR) on a guarantor is needed. The CBR may indicate if some of the business debt is in the owner's name, summarizes personal public records, and provides a summary of personal payment habits. The CBR also includes a credit score based on the payment history, number of open accounts, length of time at an address, and other personal information