

# Informita News

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## Will AI change Accounts Receivable?

For many years, software companies have been hailing the revolution that is about to happen because of a key piece of technology that they are touting. That is not to say that there hasn't been a serious improvement in AR processes in the last 30 years, but the changes have been incremental over that period. But every software company that you can think of always claims that its software solution will improve working capital. The latest in this wave of hype is artificial intelligence. We all read articles trying to scare us to death that AI is going to take all our jobs away or that it is going to create an opportunity for cost reductions unheard of since the beginning of the industrial revolution. Somewhere in between is probably closer to the truth. Let's take the AR department as an example. In any company, the basic process of issuing an invoice and having the customer pay that invoice should be remarkably simple. And that was true before we had any computers. The technology age has allowed for numerous advances, such as computer-generated invoices, electronic transmission of those invoices, electronic payment, and direct debit, amongst many other advances. Then came serious business-oriented software. The ERP revolution of the 1980s and 1990s promised that accounts receivable would be transformed by the new technology. It was improved mainly by the advent of automated bank reconciliations being available to almost all companies, but it was not transformed. The specialist AR software came out that, claimed that their version of customer segmentation would help AR collectors collect more cash. It turns out that many of these segmentation methodologies are more to do with customer risk than collection performance. About 10 years ago software companies started talking up the AI capabilities of their software. It turned out that this was just marketing hype. More recently, these software companies tell us about Generative AI. It turns out that these are very fast computer programmes that can crunch gigantic amounts of data really quickly, but they are not really artificial intelligence. The basic problem for all the software vendors is that they do not really understand how AR works. The reasons that we need an AR department is to process documentation, call customers who have not paid and help fix the process issues that prevent a bill from being paid. Technology has done a great job of reducing the amount of human intervention required to process documentation and payments. And advances in these areas continue. But there has been very little impact on the human factors that create the need for AR collectors. Not every customer pays on time and things go wrong that need to be fixed. As humans we make mistakes, we have a habit of misinterpreting each other and making false assumptions. As long as we do this, there will be a need for another human to intervene to smooth things out. AI will be useful but not a magic bullet.

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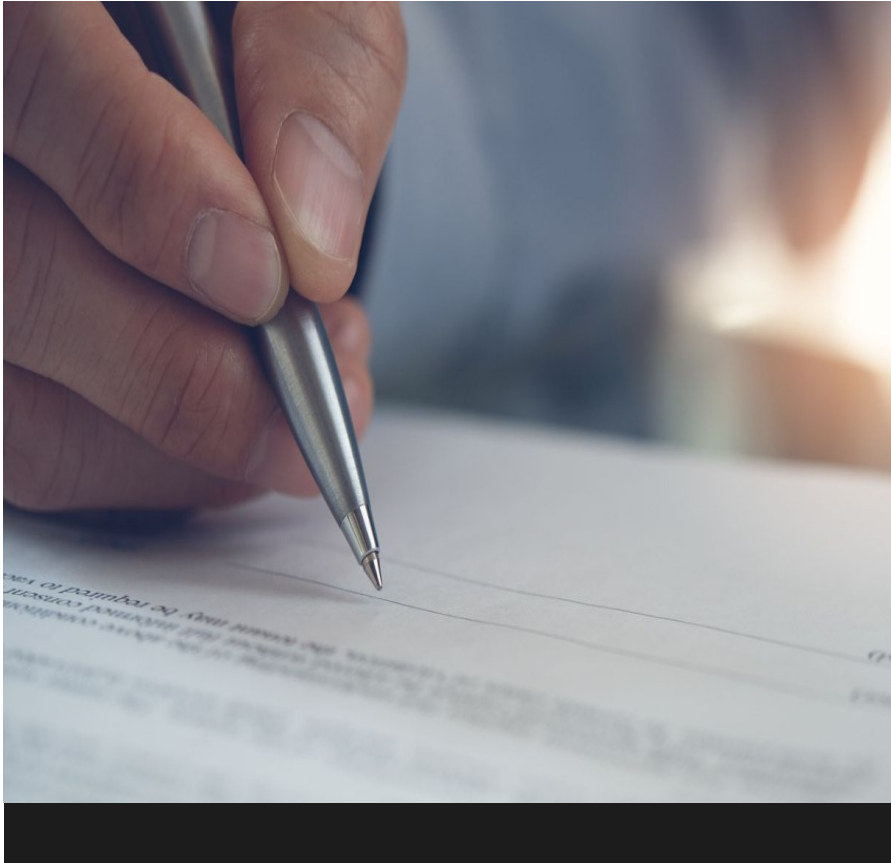
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## Customer Credit Policy

Why is it important?

There are usually three essential elements to having a good Day Sales Outstanding (DSO). The first is having a clear and enforced customer credit policy, the second is to credit check your customers effectively, and the third is to have an efficient collection process. The second and third parts are the usual ones pushed by software companies since they are processes that can either be automated or supported by good software programs. But if you have good collectors and effective credit management, you can still have a high DSO because the commercial team gave inappropriate terms to the customer. This is far more common than many think. An effective customer credit policy needs to set out the rules of engagement with customers in a very simple way. Salespeople are often not financially trained and may be confused by complicated finance terminology and concepts. The policy needs to be clear about what the standard payment terms and conditions with the customer should be, and who is allowed to authorise exceptions. But even a good policy document needs to be enforced. The consequences of breaching or ignoring the policy need to be very clear. Senior management needs to be fully prepared to enforce the policy rigorously and without exception. For most commercial people, they will accept the rules they are given, but there is always an unruly minority. From these people, expect the excuses that the credit policy will destroy the business (never true), and after that, they didn't understand the policy correctly. When the policy is breached there needs to be disciplinary action that is transparent and fair. Usually, this will mean the end of any dissent, and then the business will settle into a new equilibrium.

## Duplicate Payments

What's the problem?

In 1997, I found myself in a room in Troy, Michigan, where my client colleagues were discussing "Dupe-Checks". Not knowing the term, I wondered why they were discussing the 1968 Prime Minister of Czechoslovakia (Alexander Dubček). But of course, they were discussing nothing of the kind. In fact, the conversation was about the number of duplicate payments made to suppliers. It seemed simple to me that you should create a report detailing all the potential duplicate payments, then go check the invoices to see if they really are duplicates and then go to get the money back from those who were double paid. In reality, this was outsourced to a third party, who did all those things and then took a large percentage of the cash collected from suppliers. In addition, they deliberately did not suggest any process fixes to prevent future duplicate payments since they had a multi-year contract to repeat the process and make more money. The right thing to do is to fix the process and not chase the dragon.





## China: Getting paid

How difficult can it be?

In recent years, China has proven to be a difficult place to do business. Several things are affecting the economy, such as the property crisis, African Swine Flu and now the international trade situation. This can happen in any country, but China is a place that has its quirks in how business is done and how one partner is favoured or disfavoured over another. Since the pandemic, it has become much trickier to get paid on time. The bankruptcy rate is very high, and the number of firms that are not technically bankrupt but are very short of cash is increasing. So it is much more important than ever to understand your customers' key commercial relationships. If their key partnerships are with government entities or government-controlled entities, things are usually fine, but otherwise be careful.



## Iraq: How messy is messy?

While the days of all-out war in Iraq are long gone, Iraq remains a complicated place to do business. It used to be that the Kurdistan region was easier to do business in since it controlled its own oil money, and business could be easily conducted through Turkish banks. This is no longer the case. Anything paid for in US dollars needs to be authorised by the Iraqi Central Bank, and all oil revenues are now controlled from Baghdad. That is not to say that there isn't business to be done. There are many sectors that are crying out for imports of all kinds, but getting paid remains a big problem. The Iraqi economy is still recovering from the effects of multiple wars and many decades of bad and corrupt government. The banking system is still extremely underdeveloped, and many companies exporting to Iraq still prefer to be paid in advance of delivery. There is progress on the payment system, but it is proving to be very slow.

## Trade agreements

The traditional process is that trade agreements take years to negotiate, get into minutia about how an agreement can be practically implemented and then needs to be ratified by parliaments in the countries affected. This can be an extremely arduous process where the ultimate outcome is by no means certain. A good example would be the agreement between Mercosur and the European Union. Talks began in 1999. An agreement in principle was reached in 2019. The final chapters of the agreement were agreed upon in 2020. As we speak, the agreement needs to be ratified by a qualified majority of the 27 EU member states. As we stand, there is no agreement in place on the ground. The contrast is the approach taken by the current US administration. Their style is to threaten high tariffs, negotiate on some high-level points and leave the boring details for later. Agreements are proving hard to implement since there is very little detail for the people on the ground to work with. Anyone in the import/export business will tell you that without the necessary detail on procedures, trade will simply stop. Suppliers will always take the path of least resistance and least cost.

## Using AR to secure debt

What bankers really want?

There was an old Bob Hope quip that stated that banks only lend money to people who don't need it. True or not, the one thing that is always a fact is that when banks lend money to people and businesses, they want adequate security to cover the loan. That could be fixed assets such as buildings, sometimes it can be items of stock, and very often debt will be securitised against accounts receivable. This is slightly ironic from a working capital perspective, since if you want to maximise cash flows, you should be reducing accounts receivable. However, from a bank's perspective, they want the asset as security for the debt that you will pay interest on. This all goes to prove that banks have no real interest in helping their customers manage working capital in any efficient sense; they just want you to incur debt, pay for the privilege of having that debt and ensure that if everything goes wrong, their money is secure. In our experience, there have been a few cases where potential clients acknowledged that they had a major problem with accounts receivable, only to back out of a programme since their short-term cash flows were secured against the very same ballooning accounts receivable. This is not to say that having overdraft facilities are not a good thing for businesses. They are, but there can be a danger that you get sucked into a never-ending cycle of debt when the underlying issue is never resolved.



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