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What Is Credit Management?

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If you own a business, you know that you occasionally have customers who owe you money—and that you sometimes struggle in your attempts to collect that money. You appropriately become frustrated with not getting paid after you complete a job. Perhaps you ship an order and then have to make collection calls, or maybe you just ignore the problem and hope the bill will eventually be paid.

Smart company owners learn how to collect the money that is owed them. They also know how to prevent accounts from becoming past-due, and how to keep their customers on track with less effort. That is what is called credit management.

Credit management is the process by which you control your business's credit, accounts payable, and receivables. Correctly managing your business's credit entails creating an outline of policies and procedures that will provide your customers with options when they cannot pay in full and on time. Effective credit policies provide an outline or plan that will enable you to adequately provide reasonable credit limits for customers who have revolving credit. This plan would also include procedures on how to deal with past-due or late-paying accounts, as well as advice on how to eliminate them from the books. You want to have guidelines to legally collect money owed to your company that has been lost due to late payers, nonpaying customers, and bad checks. You also want to establish a streamlined system that will maintain timely contact with all of your late-paying customers. These procedures help you to be aware of when accounts are becoming past-due and to help you avoid carrying bad debt on the receivables.

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Business owners all have different types of companies in various industries, all of which can extend credit. Therefore, it should make sense that no two credit policies will be the same. One major difference is that which exists between a service or retail business. Your credit policy should use multiple facets to cater to prospective customers but also protect you and your organization.

You are limited in what you can and cannot ask a prospective customer in order to extend them credit. You need to be aware of what these questions and the associated laws are before you create your credit policy, which will help to filter customers so you don't have to spend your time chasing your money. The best credit policy is short, easy to understand, and to the point; it should avoid long-winded statements with a lot of legal terminology or big words. Always create your policy and forms with the customer in mind—the easier and the clearer, the better.

OBJECTIVES OF CREDIT MANAGEMENT

If you don't have a credit policy for your business, everyone will want to buy from you, which can result in unpaid and past-due invoices on your books. In order to be effective, your credit policy must meet the following objectives:

- Effectively outlines policies and procedures that will help provide your customers with options when they cannot pay in full.
- Implements a plan that will enable your business to adequately provide reasonable credit limits for your customers that have revolving credit accounts.

- Outlines the steps to take to collect from past-due or late-paying customers and how to eliminate bad debt.
- Provides guidelines to legally collect money that is due to your company from slow or nonpaying customers and from bad checks.
- Exacts a streamlined system to deal with any past-due accounts.

Once you've established your credit management policies or procedures, you will know how to maintain your cash flow to benefit you and your business—and how to get customers to pay easily and quickly. The longer you wait to take action on getting paid, the lesser your chances are of receiving any money. A credit management plan maintains your customers' satisfaction and insures reliable payment of accounts, and the credit policy sets a positive credit tone for your business. It also lets potential customers know that you are serious about your business, and lets you control your customers, cash flow, and profits.

It is up to you how tightly you wish to enforce your policy. You can have a very strict credit policy—which alienates some customers—or a looser policy if you are willing to take a bigger risk. Some business owners have more flexible credit policies for a variety of reasons. They may want to open several new accounts quickly, they might be a large market or a competitive industry, or they may offer less discriminating credit terms for a limited time to introduce a new service or product. Or they may simply have a large inventory in a warehouse and want to move it quickly.

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Whatever your level of stringency, any successful in-house policy must:

- Be tough yet flexible
- Have specific action guidelines
- Be enforced consistently

Proper and regular attention involves developing a collection procedure or policy and following each step fully before moving on to the next step. It means that you never move backward or repeat a step in the hope of salvaging an account. You need to be firm with policy enforcement and attentive to your policy's details.

Good credit management is crucial to your business. If you can't manage the cash and credit that flows through your company, it will inevitably fail. You must respect your cash and deal with it properly in order to be successful.

Some business owners feel that it's easier to process orders just by obtaining limited information on the customers. Many new entrepreneurs are so excited to make the sale that they don't want to offend the customer by asking them to fill out a credit application. Their next mistake in this situation is not asking for the money when it is due. They were so thrilled to make the sale that they're afraid to anger the customer by asking for the money—even when it is past-due. They don't realize that this means that they actually *failed* to make the sale in the first place.

Take a different approach here by showing potential customers that you are proud of what you do and serious about your business by asking them to fill out a credit application. Any customer who takes offense to this or refuses to fill out

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the application is probably not creditworthy—and is one you wouldn't want as a customer anyway.

Most business owners don't realize that a credit policy is a method to control their bottom line, sales, and income. Using this tool to increase your sales and profits is a smart maneuver that many companies unfortunately ignore. A credit application a potential customer fills out provides near-perfect information about them and how they pay their bills. It also helps you decide if the customer can afford more credit.

Be warned that when you utter the word "credit," the first thing that comes to most people's minds is "bad." Credit has a variety of different meanings. This book focuses on both your company's and your customers' credit—a combination of which can sometimes result in debt. In fact, over 70 percent of American consumers that use credit cards have no idea what interest rates they are paying; that's a pretty scary fact!

Most people's credit problems are unexpected. People generally do not buy items on credit with the intention of not paying and just running off into the sunset (okay, maybe a few do). However, some of the most common causes of credit problems are:

- Unexpected medical bills
- Lack of savings
- No experience dealing with money or a budget
- Unemployment
- Overextending oneself financially
- Accidents or emergencies
- Separation and divorce
- Death of a spouse or other family member

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Developing an understanding of the most common causes of credit problems will help you be more effective in trying to collect money that is due to you.

People use credit for many different things that range from quieting children to keeping up with the neighbors. Many consumers believe that the more credit you have, the more successful you are. For example, the platinum card makes us feel special, or a gold card means we are better or more successful than our neighbor who only has a silver card. A lot of people don't want to be limited by living within their means. They want more, and they want it now—and they are bringing their children up the same way. Someone who uses a credit card to fulfill that dream when they can barely make ends meet is essentially making a deal with the devil. However, you can help control this problem by assisting your customers in making the right choices. You can do this by limiting their credit to what they can afford, thereby benefiting both your customers and your business.

HOW CREDIT MANAGEMENT AFFECTS YOUR CUSTOMERS

Your credit management plan is a two-way street; you create the rules and your customers have to play by them if they want to do business with you. If your customers don't follow your rules, they are out of the game. It is your job to be fair, reasonable, and follow the law to ensure your customers will not be intimidated by your credit policy and will continue to be good paying customers who refer you to others.

Some customers with a history of bad credit look to buy specifically from companies where they don't have to fill out a credit application or any type of new account forms. Any customer who balks at filling out any new account information should be established as Cash on Delivery (COD) or prepayment only. Never extend credit without getting at least a signed credit application and checking references. A quality customer will not run away when they have to fill out any paperwork, and will be glad to see that they are dealing with an organized, professional business. They will feel more secure doing business with you and will appreciate how serious you are about keeping your company profitable. This elevates your organization in the customers' eyes; they will know you are an upstanding business owner with values and will want to continue to interact with you.

Extensive research found that consumers who can obtain credit will even pay more for a product or service when they are extended credit and have great customer service. Faster, easier, and smoother procedures will garner the most sales and better paying customers. The result is more transactions, more income, and happier customers. It can also prompt free and valuable word-of-mouth advertising from satisfied customers.

Knowing the types of customers you have can also help you to limit your credit risk. Your customer base can be compiled by many different types of people with different needs depending on the type of business you have. However, you should be aware of the following individuals, as they will almost surely put you at risk:

- *Slow payers* who are forgetful or unorganized.
- Those who "*want to pay but can't*" due to economic circumstances.

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- Those who *are able to pay but unwilling* due to a dispute or complaint.
- *Credit criminals*: people who commonly apply for credit, then don't pay or find a reason not to pay.

Make sure the credit applications you give new customers are simple and to the point. Jamming too much stuff onto applications and forms scares away potential customers—especially if they can go somewhere else, fill out one easy form, and get the product or service they're seeking right away. Customers are distracted by long forms, especially those full of legal jargon, long technical terms, or that ask for too much information. Keep the forms short and the language easy to understand.

Customers, creditors, and business owners can assess your business's credibility based solely on your policies. If you extend credit without making sure the proper application is filled out, customers know you aren't serious, which could lead to collection issues down the road. The first step is to design a customer-friendly policy that ensures you have the information you need if there is ever a payment problem but also a policy that doesn't scare away your customers. You must maintain amicable customer relations while protecting yourself and your company from potential financial adversity. The second step is to make sure that the policy is in effect *before* obtaining new customers, and ensuring that everyone in your organization is familiar with and enforces your policy. It is not very professional to be searching for a credit application or not know which forms they have to fill out in order to open a new account.

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If you come to realize that your credit application is not working for you—or you are having problems with some aspect of your credit policy—you can change it at any time and measure your results to be sure the new approach is an improvement. The best strategy for ensuring an effective credit policy is to look at your bottom line and talk to your customers. Are most of your credit-approved customers paying on time or are you extending credit to customers who are paying slowly or not at all? Are your customers having any problems or questions with the forms or the information they had to provide? Keep asking these questions; it will enable you to tweak your policy so that it is streamlined and working as efficiently as possible.

The following are some steps you can take to make your credit policy easy, quick, and painless.

- *Make it easy* for the customer to get credit with you. Have packets paper-clipped together at the front desk; include the credit application, automatic payment permission forms, and anything else you want filled out before opening an account. You can print out these forms and clip them together or put them in a clipboard and hand them to every new customer to fill out. Make it a policy of yours and your employees and you should never make an exception.
- *Make it quick* by having these packets ready and waiting for anyone who comes in. Have pens and clipboards available so the forms can be filled out immediately.
- *Make it painless* by either having them wait and checking their credit application while they are present or

responding to them within a certain time period, say 24 hours.

Like everyone else, consumers today expect convenience and speed. You risk losing a customer if you make the account-opening process too difficult or unorganized.

ELEMENTS THAT AFFECT CREDIT MANAGEMENT

It is important that your customers know your credit policies and payment terms before they begin interacting financially with you. Reiteration of your credit policy and procedures when payment is overdue is a good step to take in trying to obtain payment. Once you extend credit, it is important to maintain accurate records on an account's payment history—and always adhere to your collection policies, no matter what events transpire. You cannot predict the future or changing market conditions. To anticipate economic fluctuations, try to keep current with trade reports pertaining to specific companies and industries. And *always* ask for payment when it is due. You should have procedures in writing for your employees as well as your customers; you might even consider framing a copy of the procedures and hanging it in your lobby or waiting room.

Customers who are approved for credit will buy more if they can pay later, so make the process as streamlined as you can. Another option is to advertise a free gift, in the same way that banks might offer an incentive such as a free toaster or blanket when you open a new checking account. Consider providing something such as a discount for credit-approved customers in a certain time frame. For example, "Get

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25 percent off your first order if you apply for a credit account and are credit-approved between January 1 and January 14." It's a good idea to offer this type of deal to existing customers as well.

You only need credit management or a credit policy if you extend credit and your customers keep coming back. A good idea is to take a look at your competition and get an idea of what they do for credit-approved customers. Do they have a credit policy? If they do, what is included in it? What does their credit application look like and how long does it take them to process? You can find most of these answers online, since many businesses post this information on their websites.

WHAT IS CREDIT RISK?

Credit risk is the hazard of loss due to a default on a contract, or more generally, due to some "credit event." This has traditionally only applied to situations where debt holders or business owners were concerned that the debtor or customer to whom they made a loan or extended credit might default on a payment. For that reason, credit risk is sometimes also called default risk.

Almost all companies carry some credit risk, because most organizations do not demand upfront cash payments for all products delivered and services rendered. Instead, they supply the product or service and then bill the customer, often specifying their terms of payment. Credit risk is the time between when the customer receives the product or service and when you get paid.

Businesses were asked in a recent *Wall Street Journal* poll by icsolutions.com, "Are your customers taking more time to

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pay for your companies' goods and services?" Seventy-eight percent said yes, and 23 percent said no—results that clearly indicate an increase in customers paying with less speed. This is precisely why it is so crucial that you learn how to limit your business credit risk so that you can survive while customers take longer to pay.

WAYS TO LIMIT YOUR CREDIT RISK

The following are a few tactics you can employ to decrease your chances of running into problems in this area.

Invest in Education

Continue to educate yourself and your employees about the latest events in your industry. Attend seminars, free online webinars or tele-seminars; read books and trade magazines; and keep up to date on what is happening in your industry. Learn all that you can through whatever means are available to you.

Network and Make Contacts Online and Offline

Networking will keep you on everyone's minds. This way, if you end up losing your job you will have a slew of business cards of others in your field that you can contact during tough times.

Follow the Market

Read the newspapers or watch the news. Be aware of what is happening—both within your industry and in general—and stay on top of it.

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Pay Off Debt

If you can pay off any debt, now is the time to do it. Dealing with a recession is hard enough without a boatload of debt to cause your stress level to go through the roof. Pay cash for anything you need. If you don't have the cash, ask yourself if you really *need* it or just *want* it. Try not to use credit cards (unless you pay them off in full each month) until you fully establish your company in order to build up your business credit.

Cut Back on Extras

This might seem like a simple suggestion until you really think about what it entails. For example, do you need all the bells and whistles you have on your business phone? Do you need a coffee service in your office or can you buy a coffee pot and brew your own much cheaper? Can you bring a bag lunch or carpool to work? There are countless ways to save a little here and a little there.

Build Your Online Presence

Create a website, blog, newsletters, or articles. Join online networking groups that relate to your industry. Mentor someone or find a mentor for yourself or your business.

Have Your Clients or Customers Sign a Long-Term Contract

This is always a good idea. Or, another option, review existing contracts and either renew or extend them.

Specialize in Something

Make yourself and your company known as the experts or go-to people for a particular area of service. This will highlight your value, and employers are more likely to keep an employee who can do more than one thing.

You might find yourself with more time or feeling frustrated that you can't make more sales when business is low. Take that time as an opportunity to follow what's going on in the market. Read newspapers or watch the news, know what is happening with the economy, and stay aware of the latest developments. You'll relieve your frustration and improve your ability to forecast events that affect your business as you become more educated. Now is also the time to network and make sure your business stays on everyone's mind. Make contacts on- and offline to bring in more sales.

The following are some top tips to help you limit your credit risk.

- Give out as little credit as possible at the risk of losing sales (after all, bad credit risks aren't always worth the sale if you don't get paid).
- If you are going to extend credit, think like a banker; figure out exactly how you're going to be paid back.
- Remember that time is of the essence; get paid sooner rather than later.
- Have the facts in front of you before making a collection call.
- Be willing to negotiate.
- Hire a collection agency. (This is covered in more detail in Chapter 8, Third Party Collection Services.)

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MANAGING CREDIT RISK

Managing credit risk is important for any company but especially for new or small businesses. Larger companies may have the advantage of a credit risk department whose job it is to assess customers' financial health and extend credit (or not) accordingly, much like a credit manager. For example, a new business that is selling its products to a troubled customer may attempt to lessen risk by tightening payment terms from "net 30" to "net 15," by actually selling less product on credit to the retailer, or even by cutting off credit entirely and demanding payment in advance. The business might lower the existing credit limit and rerun the credit application to reevaluate the credit risk factors. Though this might cause friction in the customer relationship, the company will be better off taking this approach with customers who are late in paying their bills. This is certainly the case if clients default and you have to place the account for collection, if you have to take them to court, or if they file bankruptcy.

On the other hand, credit risk is not really manageable for very small companies with only one or two customers. This makes these companies very vulnerable to defaults or even payment delays by their customers. If a business with only two or three customers hasn't limited their risk, they could find themselves unable to pay bills or get paid if just one of those customers is late in making a payment or goes out of business. This is an area in which it's particularly important not to put all your eggs in one basket. Establishing a broader customer base can help you extend credit while limiting your risk and managing your cash flow.

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Some things you can do to limit your risk with existing customers are:

- Get a personal guarantee
- Offer month-to-month credit
- Offer ship-to-ship credit
- Ask for a security deposit to keep in a trust account in the event the customer does not pay an invoice
- Get a 50 percent deposit on every order and make sure the balance is paid upon order completion

The best approach here is to make sure that you get to know your customers as well as possible. In order to limit your risk but make your credit policy effective, you need to implement a procedure for any new or credit-approved existing customers. You should learn what your customers are looking for when they apply for credit with your company. It's simply good business to cater to potential new customers; the easier you make it for them to spend more money with you, the more money and sales you acquire.

You want to take steps to minimize your exposure to high-risk debt to limit your credit risk. You may have noticed that many banks and lenders have established much stricter guidelines recently for applying and being approved for credit lines than in the past. Bankruptcies are expected to continue to soar in the coming year, and revolving credit is becoming much harder to obtain. Revolving credit is a type of credit that does not have a fixed number of payments. An example of revolving credit is a credit card as opposed to a car loan, which would have a fixed number of payments.

Some things you can do to tighten your credit policy belt are:

- Be clear on the terms of your deal; get it in writing!
- If you extend credit, monitor the accounts for overdue payments, and keep them up to date.
- Have a penalty for past-due balances, such as a late fee or termination of credit privileges.
- Research collection agencies before you need one.
- Have every customer sign a credit application and *check their credit*—thoroughly!

The following are questions to ask yourself about your delinquent customers in order to limit your credit risk:

- Are they in a position to pay in full?
- Will they be in a position to pay your bill in six months?
- What will you do if they can't pay you?
- How will you pay your bills if your customers are delinquent?

What is your next step when your customers cannot pay you because of a job loss or other economic effects? Make sure that you follow the laws in your state to collect the money that is owed to you, even when things get tough. Be aware of the parameters in the Fair Debt Collection Practices Act (FDCPA) and treat your customers as you would like to be treated. Be sure to follow these rules, no matter how frustrated or upset you get.

- Do not berate or belittle the customer.
- Do not swear, yell, or use foul language.

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- Do not call and then hang up on a customer.
- Do not post a notice in your office or store that some customers owe you money.
- Do not extend them any more credit until they pay you, and afterwards always get cash up front.

CHECKING PEOPLE'S CREDIT

Let's say that you have a new customer who wants to apply for credit. You must first check their credit in order to make an educated decision on how much credit you want to extend to them, or how much of a risk you want to take in terms of what you extend to them. If you have signed up with a credit reporting agency to pull credit reports, then run a credit report once you've received the customer's application. You also will want to check all references. Even though most people list references that they know are good, you should check them all anyway. Make notes right on the credit application or new account form. Call the business, personal, and bank references, and always get the full name, title, and extension of the person giving the reference. Some questions you can ask during this process are:

- How long have you known the customer?
- How long has the customer been doing business with you?
- What payment method does the customer normally use?
- Does the customer generally pay within terms, late, or early to take a discount?
- What is the customer's average balance? How many days past-due is it (if any)?

- What is the average amount of the customer's orders?
- How often does the customer order from you?
- What is the customer's current balance due? Is any of that past-due? If yes, how many days past-due?
- What are the customer's terms with you?
- Does the customer make a lot of returns?
- Does the customer take any discounts?
- What is the customer's high amount of credit in the last year or six months? Have their orders increased or decreased in dollar amounts?
- Is the customer's account current today?

When you contact the bank for a reference, you sometimes will have to fax your request on your company letterhead stating that you have authorization from the customer to request the credit reference information. You can do this easily and give the bank a call afterwards to ask questions such as:

- What type of account does this person have—business, personal, savings, checking, business loan?
- When did the person open the account?
- What is the average daily balance?
- Has the person had any insufficient funds or other returned checks? How many? When was the last one?
- Does the customer have any outstanding loans?
- What types of loans does the customer have? Are they secured or unsecured? Are they being paid as agreed?

Many new and small business owners or credit managers are reluctant to run a credit report because of the cost involved. However, you need to think of this amount in relation to what you could lose by *not* pulling the report and checking credit. The cost to run a credit report as a member of a credit bureau is an investment that is well worth it.

When checking credit and looking at someone's existing debt to decide if they can afford more, keep the following figure in mind: a total personal debt should not exceed 36 percent of a person's total income. Remember this when checking people's credit.

Unfortunately, many folks nowadays have bad debts or are financially overextended. Common financial education is nonexistent unless your parents taught you about finances when you were a kid. Though issues pertaining to debt and bills are really common sense, it's not something that is taught in schools or colleges. However, the recent recession has shown us how important these lessons are, and young people these days must learn them in order to strengthen our economy.

WHAT TO AVOID WHEN EXTENDING CREDIT

While extending credit can seem intimidating at first, it doesn't have to be. This scary element comes from the fact that you put your business out on a limb when you extend credit; you're essentially hoping that whoever you're taking on will really pay you when they promise to. Here is a list of some things to watch out for when you are considering extending credit to a customer—new or old. Avoid extending credit when:

- Someone has no credit; offer another option such as 50 percent down, balance due upon delivery.

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- Someone has bad credit; try COD or prepay.
- Someone cringes at filling out or signing any paperwork.
- Someone doesn't have a job.
- Someone doesn't have a permanent address and/or phone number.
- Someone asks to have another person, such as a cosigner, make the application.
- The applicant doesn't have a bank account.
- The applicant won't give you references.
- A check has been returned or a credit card denied.

These are just some of the red flags to look out for. When you extend credit, you put your business at risk; you therefore need to limit that risk as much as possible. You don't have to extend credit to everyone who walks through the door; plenty of your customers will be approved. So choose wisely and do your research in order to reduce your risk, and make more money.

UNDERSTANDING DEBT AND BAD DEBT

Debt is an obligation or promise to pay something on a certain date and by a certain time. It is what is owed to anyone who has extended credit to someone that has not been paid. Bad debt is what happens when someone doesn't pay their bills; it can result in their utilities being shut off or cancelled, repossession of big-ticket items like homes and cars, late fees, and being placed for collection or having to go to court.

Business owners all sell products or provide services with the understanding that customers will pay their bills. Companies that offer credit do this so they can make more money by extending credit to customers so that those people can afford their products or services. However, they lose money when those customers don't make their payments. Failing to make an agreed-upon payment after a business owner does you the courtesy of extending credit (a privilege) is disrespectful. Situations like these can cause both customers and businesses a lot of stress; customers aren't making their payments, and businesses are not getting paid—and in most cases, don't know why.

Did you know? Americans spend more than 70 percent of their gross income every year on repaying debt.

Bad debt is that which a customer has incurred and that is no longer collectible. It is therefore worthless to the creditor or business that extended the credit. Bad debt occurs once all avenues to try and collect a debt have been explored and proven unsuccessful. It can take place under a variety of circumstances; for example, when a customer files bankruptcy, dies, or skips town. It might also come about because the cost of trying to collect that debt is more than the actual debt. In these cases, the debts are normally written off to bad debt as an expense. Bad debt is normally expensed on the accounts ledger as a cost of doing business.

Though you will increase your sales as you sell on credit more often, you must make sure each customer is creditworthy. Any bad debts that you write off will reduce your net income. However, most companies have a bad debt allowance since it is unlikely that all of their credit-approved customers will pay them in full.

One thing that many company owners frequently overlook is how to prevent future credit issues that normally result in bad debt. I am always amazed at how creditors will

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hire someone to collect the bad debts they have—and then do nothing to avert future problems. It is never too late to implement a credit policy, even if you have a pile of bad debt. And the sooner you do it, the better your chances are of collecting what is already owed to you and preventing future bad debts—thereby preventing the same situation from happening again.

According to collection trends, surveys, and polls taken—as well as from my own personal experience—every debt's chance of recovery drops drastically the longer it is allowed to be past-due. The more time you let a debt sit there, the harder it becomes to collect. This was one of the reasons I charged a higher commission on any debt over one year old when I had my collection agency. Regardless of the dollar amount, the older it is, the harder it is to collect—that is, *if* you manage to collect anything at all. Many business owners either don't know or don't understand this. I have watched countless proprietors leave debts on their books for years. They assumed their customer would pay when they had the money, and avoided contacting them so as not to make them angry. After they got sick of looking at it on their books, they would place the account with my agency—and never understood why they had to pay a higher commission. Perhaps this explanation will save you from making the same mistake. Now you know that if you aren't going to actively pursue your past-due accounts, you can't let them just sit on the books. Place them with an agency right away and you will get more of your money in the long run. Another approach: If you have a large amount of bad debt, you may want to think about offering a discount if someone pays cash at the time of sale, thereby protecting yourself and saving your customer money.

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In 2008 the *Wall Street Journal* reported that bad debts have led to a change in billing—a trend that is prompting hospitals to demand cash up front from their patients. Traditionally, hospitals bill patients after they receive their care. However, with increased bad debt and charity care costs these days, hospitals want money before patients get treated. According to the American Hospital Association, unpaid bills for care given ended up costing the hospital industry $31.2 billion in 2006.

CREATING A CREDIT POLICY

When a new or potential customer asks to begin doing business with you, you should set up their account on a prepaid or cash only basis. You can then give or send the customer a credit application if they wish to become a charge customer. Once you receive the completed application, you need to check their credit and decide upon on a credit limit. If you approve the customer, you must send them a letter letting them know they have been approved, and for how much. You also have to notify them via letter if they were denied, and let them know what the reasons are. There must be a notation on the bottom of the letter telling them where they can call or write to obtain a free copy of their credit report if they disagree with any of the information.

Take the following specific steps to ensure successful credit management:

- Have every new customer fill out a credit application and/or new account form.
- Check customers' credit, and deny or approve in a timely manner.

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- Send out a denial or approval letter.
- Lock all credit forms and information in a file cabinet to which only the owner or credit manager has a key. This information is confidential and should not be available to anyone else in your company.
- Input credit limits into your computer on customers' accounts.

There are several powerful strategies that business owners can use to dramatically improve their sales, income, and bottom line. One of these is to increase awareness within your organization about your credit policy. If just one department or person doesn't abide by your written credit policy, it can completely fall apart.

A second strategy is to put one person in charge of all credit applications and new account information. All of the material you obtain on a new customer is extremely confidential. For this reason, just one employee should be handling the processing of all the new account forms and credit applications, which should also be kept in a locked file cabinet.

Speed and convenience are other important issues. Consumers today are looking for fast, easy answers. The more efficient you can make your credit policy, the happier your customers will be.

You probably know your customers pretty well—and you should. If you don't, you could very well end up with a pile of unpaid invoices and no idea how to recover the money owed on them. Don't let this happen to you.

Credit policies are a must for every business that extends credit. Any company that doesn't accept payment at the time of the sale must have a policy in place or run the risk of losing money and sales. If this gets out of control, you can end up with many customers owing you and no money coming in.

ELEMENTS OF A CREDIT POLICY

There are five major elements to any credit policy:

1. Mission
2. Goals
3. Responsibility
4. Policies and procedures
5. Terms of sale

Your *mission* is a statement of what you want this policy to do for your business. For example, your mission might be that the credit department will offer credit to all customers that fill out an application and are found creditworthy.

Each company's *goals* will differ depending on the credit policy, and they should reflect your credit department's overall objectives. Your credit department's goals might be to operate with a certain number of collectors for a specific number of accounts, while also keeping bad debt down to less than 2 percent of all sales. You might want to consider establishing new goals annually and basing them on sales, competition, and/or the economy. You could then list those goals each year in your updated policy. An example: "All customers should be contacted by phone if they become 15 days past-due, and contacted by mail if they become 25 days past-due. Any past-due accounts not having had a payment posted to them in 3 months, and that are over 90 days, will be sent to a collection agency. All credit applications should be updated and rerun every 6 months."

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Your *responsibility* should reflect the accountability or authority of your credit manager or whoever has been sanctioned to enforce your company's credit policy. For example, your credit manager would have final authority to check and either approve or deny customers' credit, credit limits, revoke credit, or put accounts on hold. This section would state the duties of all related personnel.

Your *policies and procedures* would list how everything will work within the credit function. This includes your payment terms, new account processes, credit applications, checking credit, pulling credit reports, setting credit limits, when and how to contact customers, making sales when a customer is past-due, disputes, bad debt, and using a third party collection agency as well as all other issues relating to the credit and collections function. An example of a policy might be that you will not grant a customer a line of credit unless they've completed and signed a credit application. Another could be that accounts can only be placed with a collection agency upon approval of the sales department or VP of Finance.

Finally, your *terms of sale* are your payment terms—including how and when you want to get paid, as well as the parameters you've listed on your credit applications, invoices, statements, and website. You would just list your terms, for example "net 30," and all other terms or discounts must be approved by the credit manager. There are six steps you need to take as part of your policy each time you have a potential new customer.

1. Completing the new account form
2. Completing the credit application

3. Checking credit
4. Setting credit limits
5. Notifying the customer
6. Updating credit limits

Though the new account form is not required, it can be an incredibly helpful way of gathering general information such as name, address, contact information, how the customer heard about the company, who they currently use for this service and what their experience with them has been, and why they want to change companies. Knowing what potential customers want and didn't get from another company lets you provide great service to them. By comparing customers' experiences with other companies, you gain an advantageous insight into customer satisfaction.

If you don't implement a credit policy or credit management plan, do make sure that you always get a signed credit application. This single document will help you in so many ways if you ever have a problem with the customer—for instance, if their phone becomes disconnected, their mail is returned, or you have to take them to court or place them with a collection agency or attorney. The application will have all the information a third party will need in order to investigate the customer, contact them at work, or locate them if they have skipped town. It also provides a Social Security number to help with credit reporting.

You can check credit in a few different ways. One is to become a member of one of the credit bureaus and pull credit reports. Or you can manually check credit by calling references, vendors, banks, and anyone listed on the credit application.

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It's certainly tougher to set credit limits without a credit report, since you have to determine on your own what salary this person makes and what their expenses might be. You don't know if the customer has any credit cards, whether they are past-due, or even if they have been placed with a collection agency before.

It's also a good idea to recheck customers' credit once or twice a year. Similarly, if you read something in a trade journal or newspaper about a company having financial issues, you might want to review their account and reevaluate their credit limit. Keep in mind that if you do change the credit limit in either case, you must notify your customer and tell them why.

Below, you'll find an example of a credit policy that has each of the elements mentioned above. Take a close look at each component to see how they work together to form a cohesive plan.

CREDIT POLICY FOR ABC COMPANY

Mission

The Credit Department will offer credit to all customers that fill out and sign a credit application and are found to be creditworthy.

Goals

The Credit Department's goals are to operate with one collector per 700 accounts while keeping bad debt down to less than 2 percent of total sales.

All customers found to be 15 days past-due will be contacted by mail.

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All customers found to be 20 days past-due will be contacted by phone.

Accounts over 90 days old with no payment activity in the previous three months will be placed with a collection agency that has been approved by the credit manager.

All credit applications will be updated and rerun every six months.

Responsibility

The Credit Manager has full authority over all aspects of the credit and collections functions.

The Credit Manager reports to the Chief Executive Officer.

Policies and Procedures

No customer will be given a line of credit without completing and signing a credit application.

Customers' terms cannot be changed without the Credit Manager's approval.

No accounts may be placed with a collection agency without the Credit Manager's approval.

Accounts looking for a credit limit higher than $5,000 must be approved by the Chief Executive Officer.

Terms of Sale

Two percent 10 days, net 30 days.

$25 fee on returned checks.

Court costs and collection fees can be added to balances placed with a collection agency or taken to court for payment.

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All other special terms or discounts must be approved by the Credit Manager.

SKILLS AND RESOURCES NEEDED FOR SUCCESSFUL CREDIT MANAGEMENT

You want to make sure your credit management plan covers these six areas:

1. How to apply for credit
2. Late fees, interest fees, collection, court, or bad check fees
3. Repayment terms and conditions
4. Credit limits
5. Buyer responsibilities
6. Seller liability

There are certain tools that are essential for a credit manager to effectively do his or her job. An absence of just one of the following tools can provide a crack through which a debtor may slip.

- Signed credit application
- Full knowledge of the FDCPA and additional state laws
- Communication skills
- Negotiation skills
- Skiptracing or location skills
- Mediation skills
- Organization skills
- Creativity
- Flexibility

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There are a few areas in which you might consider getting professional training. Some of these are developing your telephone voice, refining your listening skills, managing the emotional side of debt collection, organization prior to making any calls, preparing your opening statement, and closing the call.

Normally, credit managers are responsible for managing all lines of credit, providing account and payment support service to customers, evaluating credit risk, assessing new customers' creditworthiness, and authorizing new revolving credit accounts. It is also their job to negotiate terms and conditions to minimize risk exposure, manage any customer disputes, keep customer records and credit applications, set credit limits, review credit performance of accounts, enforce a credit policy, and improve cash collections.

Clearly, credit managers must have strong communication and organizational skills, and be able to solve problems in a positive way.

Having been a first-party and a third-party bill collector—and having trained collectors for both positions—I know from experience that the most difficult aspect of being a collector is dealing with debtors either on the phone or in person. In my view, the most important part of collecting is following the laws—especially since they keep changing—keeping your cool, and staying in control of the situation so you can get paid. I've found that the best way to achieve this is to be educated. If you know the laws and prepare responses for debtors' potential excuses or comebacks, you will be able to answer the debtor no matter what the scenario and, even more important, offer a solution. One of the ways I approached this with the collectors that worked for me was to test them on the laws and have them listen to me make collection calls. I provided them with charts for their desk with common excuses and examples of replies. The more collection calls you make, the better you get at it and the more experience you will have dealing with common excuses and how you should respond.

FOLLOWING FEDERAL AND STATE LAWS

It is simply good business practice to know what laws are out there—even if they do not necessarily apply to you. One law that applies to third party collectors and attorneys who regularly collect debts for others (but does not apply to business owners collecting their own debts) is the Fair Debt Collection Practices Act. The FDCPA was created to protect consumers and became effective March 20, 1978. Being aware of the FDCPA provides you with structure and guidelines for your credit policy. If you learn and follow this law, you will see that you will have much more success collecting from your customers.

Another law, called The Fair Credit Reporting Act (FCRA), originally passed in 1970, was designed to promote accuracy and ensure the privacy of the information used in consumer credit reports. This law ensures that consumers have access to information about them that lenders, insurers, and others obtain from credit bureaus and use to make decisions about providing credit and other services. The FCRA also requires that users of credit reports (which would be you if you wanted to check credit through use of credit reports) have a "permissible purpose" to obtain them. It also mandates that credit reporting agencies maintain the security and integrity of

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consumer files, and allows consumers to limit certain uses of their reports. Your "permissible purpose" would be to extend credit—thus the importance of a signed credit application.

WHY SHOULD YOU HAVE A CREDIT MANAGEMENT PLAN?

There are so many reasons you need this. A credit management plan, for example, does the following things:

- Provides timely notification to your customers regarding any past-due amounts, therefore eliminating old balances from being carried as receivables.
- Outlines a procedure that will provide your customers with options when they cannot pay in full or on time.
- Establishes a procedure on when and what to do with small balances on customers' accounts.
- Enables you to adequately provide reasonable credit limits for customers with revolving credit accounts.
- Sets guidelines to legally collect money due to your company that was lost because of bad checks.
- Establishes a system that will maintain timely contact with your customers when their accounts are past-due. It also provides a procedure that enables your business to keep credit card numbers and checking account information on file for customers and automatically charge them when they place an order or for scheduled monthly or weekly payments.
- Makes your business aware of when an account should be placed for collection and thereby helps you avoid carrying bad debts on the receivables.

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- Eliminates orders being held for nonpayment and will better service customers in a timely manner.
- Alerts you as to when to write off a balance to bad debt.

Having a credit management plan in place can help your business be successful, make more money, and more sales. Credit has traditionally been used to allow individuals to live beyond their means, or because some are not dedicated enough to save money for something that they want *now*. Many people have a cavalier attitude toward credit and seem to feel as though it is owed to them. Keep in mind as you work on your credit management plan that credit is a privilege that you as the business owner extend to customers you find worthy of it.

People apply for credit for all sorts of reasons. For some, credit fulfills self-esteem issues by enabling them to "buy" friends by picking up the check or paying for movie tickets when they don't really have the money. Some use credit for a feel-good activity such as shopping (the number-one feel better activity when someone is depressed or sad). Even the most educated people with very good jobs and big paychecks get so far into debt that they file for bankruptcy and fall into a depression. Credit problems are not "poor" or "rich" person problems; rather, they are a people problem that frequently stems from personal issues. Consider the following transformation in credit trends:

Then: People used to be ashamed to file for bankruptcy.
Now: Many people suffer from credit card dependency and there is no longer any shame in being in debt.

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USING CREDIT MANAGEMENT TO IMPROVE COLLECTION PROCEDURES

I've written countless credit policies for a variety of businesses—large and small, retail and service—policies that have helped them all to make more money. People frequently ask me what my books can do for them—and who exactly needs these books. Some potential answers are:

- Anyone who wants to start their own business.
- Driven and ambitious people who like to see the results of their work.
- Business owners who have money owed to them.
- Business owners who do not have a credit policy for their business.
- Entrepreneurs who want to be their own boss and make their own future.

Using this book for your business will help you collect money from your customers in a fast and effective way. You'll be able to see the actual results of your work reflected in your bottom line. You will collect more money and be more successful. You will learn how to weed out and fire slow or nonpaying customers that are dragging you and your business down.

Now for the most popular question I am asked: "How do I create a credit policy and why do I need one?"

A credit policy is just as necessary to a company as a business plan or a marketing plan. Without a business plan, you won't be able to get a loan to start your company. If you don't have a marketing plan, you will not have the media exposure you need or a way to get the word out. And if you don't have

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a credit policy, you will not be in control of your cash flow or your company's success. Any credit policy you create should be included in your business plan, along with your marketing strategy. The bank that you approach for a loan will see that you have done your research and that you are very serious about your business, how it will be run, and how you will be making money to pay them back. Incorporating your credit policy in your business plan gives you a much better chance of being approved for a loan.

It's important to keep in mind that, just as every business or marketing plan is different, every credit policy is different as well. It is based on your goals for your company and how much money you want to make. Your credit policy has to reflect your customer service procedures, your product, and how you want your cash to flow. There are so many things to know when you create your policy, including the laws in your state and the states in which you will be doing business.

Some business owners have been running their companies for months or even years when they come to one of my talks about credit policies, limits, and applications. Inevitably, some will say to me, "I never did any of that and I have so many customers that owe me money and are past-due." Many think it is too late to do anything about it, or are afraid to ask a customer for the money or to fill out a credit application. But why worry about alienating a customer who is past-due or not paying you? This is a customer you do not need. Wouldn't you rather have a customer that pays you? Stop working for free.

If you have customers that owe you money right now, today, you can and should do something about it *immediately.*

I would bet that if you add up how much money is past-due or not being paid, the dollar amount will shock you. That alone should emphasize that *now* is the time to do something about it! The next section lists some actions every business owner can take today to start making more money by collecting what is owed to the business. Do not wait; after all, you're in business to make money, aren't you?

ACTION STEPS FOR YOU TO TAKE TODAY

1. Review your accounts receivable and find out who owes you money, how much, and how many days past-due it is. Print this list or put the invoices in a pile.
2. Set aside one hour each day to sit down and call those customers, or have someone in your office call them for you.
3. Create a series of collection letters to send out to the customers who are approaching the past-due mark or who are 30 to 60 days past-due and whom you could not reach on the phone. If you do not have any collection letters, check out one of mine, as well as forms from books for actual letters that I have used. They are very effective.
4. Mail those letters *today*.
5. Put a note in your calendar to call those people in one week if you do not have their payment. If you can't reach them by phone on that day, send another letter the same day.
6. Follow up on all phone calls and letters. If you don't do this, then don't bother to do anything, since following up is the most vital step you can take in collecting what's due to you.

You worked hard to have your own business and you deserve to get paid. Don't let your customers control your cash flow. Take the above steps and see an immediate increase in your collections.

Some other things you can do to gain knowledge or help you with collections are to network with other business owners who are doing the same thing. You can do so by joining my Credit & Collections Association and beginning to interact, exchange ideas, ask questions, and learn more about debt collection starting today. I am happy that my association is able to help entrepreneurs, credit managers, and collectors run their companies successfully and get every dollar they've earned.

Many people e-mail me questions about credit, debt collection, credit policies and procedures, and getting paid. The following is a list of the most frequent collection mistakes I've seen businesses make. In my 18 years as a bill collector, these stand out the most.

1. *Lack of a credit policy*. So many business owners do not bother to create a credit policy. They cannot expect to get paid if they don't outline how they want it to occur. This makes as little sense as making a deposit at a bank at which you don't have an account.
2. *Extending credit to anyone who walks through the door or calls to place an order.* I personally know of many business owners that do this. They are so excited to make a sale that they do not check credit, outline terms, or even get any information from the customer. Then when the person doesn't pay, or the check bounces, the creditor doesn't know what to do next. I've even met

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business owners who extended credit to a new customer without even getting the customer's last name!

3. *Receiving "non-sufficient funds" or "bad" checks.* This is the most popular yet. I cannot stress this enough: Be prepared *before* you receive a bad check. Make a sign to hang in your store or post on your website or both that tells customers what you charge when a check is returned, and what will happen to the account if a check is returned. Avoid receiving bad checks in the future by having every customer fill out a credit application—and then *check their references*!

Business owners can charge an NSF or "bad check fee" when they receive a check back from their bank. However, business owners don't know how much that fee is, and it differs from state to state. You can check my Credit & Collections website or the Law Dog website for updated bad check fees.

And keep in mind that bad check laws do not apply when an individual stops payment on a check—unless it can be proven that the check's issuer intended to stop the check when he or she first presented it for payment. Some states authorize the receiver of that bad check (you) to collect a service charge to compensate for bank fees and/or the costs incurred as a result of receiving and collecting on a bad check.

COMMON CREDIT MANAGEMENT MISTAKES AND HOW TO CORRECT THEM

If you are creating your credit policy you may not be familiar with some common mistakes made when collecting on

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past-due accounts. Make sure you don't fall into any of these traps:

- Failing to check customers' credit history before extending credit.
- Not getting a signed credit application, agreement, or contract.
- Being unfamiliar with the FDCPA and unintentionally harassing a debtor.
- Overlooking small balances.
- Not asking for the money because it makes you uncomfortable.
- Failing to know when it's the right time to turn the account over to a collection agency.
- Failing to have—and/or enforce—any type of credit policy.
- Extending credit to anyone who walks in or calls because they "sound like they will pay."
- Not taking action on returned checks.
- Not using letters and forms to collect on past-due accounts.
- Not having a credit application and having customers fill it out.
- Not checking potential and current customers' credit.
- Not understanding how to communicate with customers to keep them current with payments.
- Not using discounts and incentives to persuade customers to pay early.
- Not knowing how to set up realistic payment schedules with customers.

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- Not knowing what to do if a customer files for bankruptcy.
- Not training your collection staff properly.
- Waiting too long to use a collection agency.

Even if you've already made some of these mistakes, there are things you can do to correct them, such as taking the following steps:

- Enforce your credit policy. It's never too late for this, so start today.
- Make sure your debtors are worth something before suing them. If they don't have any assets, a job, or a bank account, there is nothing to attach or garnish if they do not pay.
- Ask for payment immediately when it is due.
- Research and sign up with a debt collection agency even before you need one and then place accounts before they get too old.

Always check credit references, and keep in mind that if something doesn't seem right, it's probably not. If you are not happy with the references provided to you, ask for additional ones. This customer wants credit from you, so *you* call the shots. If, on the other hand, you give them credit without checking them out, *they* call the shots.

Now that you have an idea about credit policies, be sure to periodically evaluate how your own credit policy is working for you and your business. It is up to you to be on top of this and to make sure you get paid for the work that you

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do. There are two easy things you can do to strengthen your credit policy right away.

1. Make sure you have a signed credit application with up-to-date contact information on file for every customer.
2. If you haven't satisfied number one, mail a new credit application to all of your credit customers along with a cover letter explaining that you are updating your files and need their current information.

Depending on how many accounts you have, number one might take you some time. If you don't have very many accounts, you will get the best results by calling the customers that owe you the most money first. Work your way down based on the total dollar amount owed. Send a collection letter with a payment envelope to anyone you don't have time to call. If you find that you just don't have the time during the week to do this, pick a night or a weekend day and make it a priority to get it done. You will be glad you did when the money starts coming in, which will motivate you to continue. If you just don't have time to do any of these things, you can still outsource this task to a collection agency. This works well because you don't pay anything if the collection agency doesn't collect anything.

Number two will help you because you'll now have a credit application for customers for whom you didn't before. You'll also have up-to-date information for customers with old applications, and will be able to reevaluate customers to make sure that their creditworthiness matches their credit limit.

I receive questions every day from business owners on a variety of collection and payment problems that they run into.

By sharing one here, I can give you an example of what other business owners are encountering and how they deal with those problems. The following story came from someone who owns and runs a locksmith company.

I run a mobile locksmith business in Colorado. Recently, a local used car dealership requested my services to make new keys for six of their repossessed vehicles. I provided them with the cost of the service in writing and had them initial this paperwork before I began the job. Once completed, I asked them what form of payment they would be using. They informed me that they cut checks on Fridays and would mail me the check. That was several weeks ago, and I have not yet received payment.

When I contacted the general manager about the late payment, he then informed me that he was not happy about the charges on my bill and would not send the payment until we renegotiated the price for my services. I informed him that he had agreed to the price before the job was done by initialing the bill/estimate and then signing the receipt—thereby promising payment—when the work was complete.

What can I legally do to expedite payment from this company? If I hire a collections attorney or agency, can I add the attorney or collection fees to the unpaid balance?

Unfortunately, the only way this man could add collection agency or attorney fees to the unpaid balance would be if he had provided for those fees on the paperwork signed by the customer *before* the job was done—and if the law in the state where the exchange occurred allows it. Another option would be to file with small claims court if the amount due is less than what is allowed; this way, the court will add any interest and fees. Once you have a judgment you can attach any assets.

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My suggestion to him would be to begin the process by sending a final demand letter with delivery confirmation. He should include the letter, the copy of the signed paperwork, and any other paperwork such as the invoice or work order in a flat rate priority envelope. He must clearly state in the letter the specific date by which he must have payment in his hands. If he fails to receive the payment on that date, he should file with the courts.

It is also crucial that this business owner not accept another payment promise that can be broken once he sends the demand letter with a specific date—and to *not* back down from that date. If he accepts another payment promise and then doesn't get paid (again!), he'll lose all credibility. If he doesn't have his money by then, he must take action. He cannot waste any more time on the account, and should immediately process it through the small claims court process or a collection agency. He can avoid this problem in the future by getting a signed contract before ever doing any work for any customer. Every business owner needs to have contracts ready and available for each customer they work with. You can have a template ready and use the same one, or customize it for each customer. But without a contract, you won't have a leg to stand on when you want to be paid.

DEALING WITH BAD CHECKS

Accepting checks as a form of payment always comes with some element of risk. Some companies don't like to deal with bad or returned checks, so they simply refuse to accept them as a form of payment. That is one way to limit your credit risk in relation to checks, and is perfectly within your rights;

after all, accepting checks is a privilege you extend to your customers.

Here are a few other things you can do to avoid getting bad checks.

- Don't let the check writer rush you.
- Don't take any check or person for granted; *always* obtain proper ID.
- Don't accept pre-written personal checks; the signature should be written in your presence.
- Don't accept unsigned checks.
- Don't accept starter checks, which are the checks a bank gives you when you open a new checking account and your own checks have not arrived yet. Starter checks normally do not have anything imprinted on them such as a name, address, or even a check number.

If you do decide you will accept checks, make sure to:

- Check that the name, address, and phone number are imprinted on the check.
- Accept checks with the *current date* only.
- Compare the ID picture with that of the person cashing or writing the check.
- Make sure the check and ID signatures match.
- Make sure the phone number is a working phone.
- Ask for a physical or street address if only a P.O. box is listed.

Writing a bad check is a crime in every state, one punishable by a fine and/or imprisonment. Yet there are an estimated 450 million bad checks written every year. This includes checks written without sufficient funds or upon accounts that have been closed. Bad check laws do not apply when an individual stops payment on a check unless it can be proven that the check's issuer intended to stop the payment when he or she presented the check. Some states authorize the bad check's receiver to collect a service charge to compensate for bank fees and/or any costs incurred as a result of receiving and collecting on a bad check. Be sure to check your particular state's statutes for the current fees or laws on what you can add to a bad check balance legally.

TOP METHODS FOR IMPROVING COLLECTION PROCEDURES

Some businesses end up having slow paying customers or past-due balances because they didn't train their customers from the beginning. You must always let your customers know about your credit policy and/or terms of payment before they even become customers. Reiterating your credit policy when payment is overdue is a good step to take in trying to obtain payment. You should also never extend credit to a new customer without having them complete a credit application and undergo the credit approval policy. It is essential to maintain accurate records on an account payment history once you extend credit, and to follow your collection policies no matter what.

Change your collection letters frequently to make them stronger and more action-oriented.

Discourage payments on account or changes in payment terms, as too many of these can impair your cash flow. Be sure to follow up right away with a letter or phone call to

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thank customers for payment when you receive payments "on account." Let them know what their new balance is, and tell them—don't ask—when to send the next payment.

On large accounts, call or send a reminder just a few days after terms if they become past-due.

Ask to speak to a manager or owner when making collection calls rather than a secretary or receptionist. You want to go directly to the decision maker.

Update your records often, and make sure you have current and up-to-date telephone numbers and addresses for your customers. You can immediately improve your collections if you follow the four steps right away with the accounts that have largest past-due balances. Let's imagine the following scenario.

You called John Smith this morning for the 18th time and left another message; also, you have found out that John recently bought a new truck and is renovating his home. When you left a message this morning, you were told John is away on vacation. You haven't collected any money from John in months and your boss is chewing you out. Since your phone calls are obviously not working, you decide to write a "Dear John" letter. Follow these steps:

1. Make the letter brief and to the point; it's best to be blunt. For example: We need to receive your payment by Friday 11/12/2012 at 5:00 P.M. Another example could be: Since we have not received a payment or a response from you, your account will be placed with a collection agency on Friday 11/12/2012 unless we receive payment in full before that date.

2. Use a larger font in the important parts of your letter—such as the balance that is due, the action you may take, or your mailing address.
3. Give a payment deadline that includes day of the week, date, and time; state what will happen on that date if you don't receive payment.
4. Send this letter in a flat rate priority mail envelope with delivery confirmation.
5. Some people worry that a priority mail envelope is going to cost extra. However, you simply pick up the envelopes for free at the post office or order them online at www.USPS.com. The postage is less than sending something by certified mail and much more effective. All of my clients that have used this approach have had fantastic results—so give it a try!

Whenever you're attempting to collect more money, remember to:

- Be confident.
- Be prepared—if you don't know what you are talking about you will fail.
- Express urgency to the customer.
- Smile.
- Listen.
- Sit up straight in your chair.
- Do not fidget or squirm.
- Focus.
- Pay attention.
- Dress professionally.

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- Present a call to action confidently and simply.
- Be ethical, courteous, and polite.
- Take notes and follow up.

You will collect more money if you have an understanding of credit and debt and how they affect your customers. To help you understand some of the things that can happen to a credit-approved customer to cause them to become past-due, I will use my own personal situation as an example. I had good credit until I got divorced. My credit went downhill as my divorce progressed. It was terrible to have bill collectors calling me and sending me letters, especially when I didn't have any money to pay them. Even though I had a full-time job, I had gone from having a two-person income to pay for my house, bills, and children down to a one-person income. Because I was the one who stayed in the home, I received all the calls. I was barely able to make my mortgage payment, pay my taxes, and then support myself and my children. Even more unfortunately, my ex-husband didn't feel the need to make child support payments; therefore, it was only *my* income that was available to me and my two young children. Since I was already working full time, I had to come up with a plan or I was not going to be able to stay in my house and care for my kids.

So I took out all of my bills and made a list of them. I then decided which bills I could eliminate in order to create more income for myself to pay my mortgage, and afford fuel for my car so I could continue to go to work and pay for utilities. Some of the things I eliminated or cancelled were cable television, my cell phone, all entertainment such as movies or going out, and unfortunately I had to find a new home for my dog. I then called the companies to which I owed money in order to explain my situation and see if there were any options. I called the electric company first, and they let me pay a small monthly amount until I could pay more. The phone company let me pay $10 to $20 a month toward my bill as long as I didn't make long distance calls or otherwise run up the bill. I then went to my town for assistance. Even though I was working full time, I had to go to my church for food—because I didn't have enough money to shop for groceries after paying my bills. Although it was admittedly pretty awful at the time, I am, in a way, fortunate since this experience helped me to be a better collector. I was able to understand where a past-due customer might be coming from, and was also able to offer advice on some tactics they could take to get out of a bad situation and pay their bills.

The following debt collection information will help you in creating your policies and procedures:

- Debtors cannot be put in jail because of failure to pay a debt.
- You can sue a debtor if they start making small monthly payments and you did not agree to accept them.
- Always record the date, time of day, name, and contact information of the person you call.
- Recording phone conversations without the consent of the other party is legal in some states.
- You cannot visit a debtor's home or call them before 8 A.M. or after 8:30 P.M.
- You cannot call a debtor at work if you know the employer does not allow this.

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- You can contact other people to find debtors, but you cannot tell them it is because they owe money.
- If a debtor gives you an attorney's name, you can contact only the attorney.
- A debtor can stop you from calling by telling you not to call anymore.
- You cannot use threats of violence, profanity, any false statements, or repeated use of a telephone to annoy or harass or give false credit information about a debtor to anyone.

CREATING AN EFFECTIVE CREDIT POLICY

When the economy took a nosedive, business owners everywhere suddenly had to deal with making more collection calls than they had been used to in order to get paid. Foreclosures are now at a record high with no quick fix in sight, and home prices in ten major metropolitan areas in October 2010 were down 6.7 percent since 2009 at the same time. People are losing their jobs in many industries. All of this is making it more difficult for company owners to collect money. Credit flow through companies is drying up at a pace not seen in decades; in fact, you've likely noticed yourself that getting credit is becoming increasingly more difficult. It is crucial for your business to keep up-to-date on the foreclosures happening nationwide and in your area.

I hope that you already have a credit policy in place and won't have to scramble to keep your receivables under control as they grow— and the economy sinks. If not, however, there is still time to take steps to help you avoid this problem in the future and take care of it now. Take a look at your

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accounts receivable listing as well as your customers' credit limits, what they owe, how old the balances are, their payment history, and the last time their credit limit was reviewed. It's essential to determine how and to whom to extend credit; it's a step that should be updated at least once a year when setting credit limits. You should also be thinking about the criteria you have for any customer to whom you extend credit. You need to remember to limit your risk while building your business.

To determine how and to whom to extend credit, you need to gather information from your customers or potential customers—and the most painless way to do this is to use credit applications. These documents give you a wealth of information that you can use later if you are having trouble getting paid, such as:

- Contact information
- Credit references
- Bank references
- Employment information
- Financial information
- Permission to check references and/or pull a credit report

Before you start telling people about your credit policy, however, you need to know your billing procedures—so you can offer them credit based on how you want cash to flow through your business. This requires you to determine the following about your business:

- Your terms
- How and when you want to get paid
- How much risk you are willing to take

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To determine how much credit to extend to a customer, ask yourself these questions:

- Do they have a pattern of paying some suppliers on time and others late?
- Is there chronic delinquency?
- Is there a seasonal pattern?
- Is any poor payment due to employment issues, a one-time event, or change in marital status?
- What are the customer's anticipated monthly purchases?
- Is cash okay until credit is approved?

And for customers who are businesses:

- Where is this company going?
- How long have they been in business?
- Who are their customers?
- What does the competition look like?
- Do they have any liens, bankruptcies, U.C.C. filings, or judgments against them?
- Have they ever been placed with a collection agency?

There are several things you can do to help protect yourself legally—as well as if you end up having to take any type of action to get paid—when you want to limit your risk while extending credit. You can get a personal guarantee, offer month-to-month credit, offer ship-to-ship credit, ask for a security deposit, and/or get a 50 percent deposit on every order.

I know that many people today are desperate for a quick fix. It may seem that many of your customers are suddenly losing their jobs or getting behind on payments. To that end,

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I have listed six easy steps you can take today to help boost your credit policy and keep your customers on their toes.

1. Print out or buy credit applications (find one at www.michelledunn.com/free.html).
2. Put them on a clipboard at your front desk or door, or on your website.
3. Have every new customer fill one out.
4. Mail one to every existing customer, with a stamped addressed envelope.
5. Check all references.
6. E-mail me with any questions: michelle@michelledunn.com.

If you didn't have a credit policy before and simply printed out a sample to start taking these steps, congratulations—you have one now. Credit policies don't have to be difficult and confusing; they can be as simple as you want. However, not having one is always a recipe for disaster—something that many companies will be discovering in the current economic situation.

Your credit policy will be based on your terms, due dates, and what you want to happen when a customer is late or doesn't pay. Some questions to think about when you are setting your payment terms are: How often do you want to get paid? Do you want to be paid upon completion of the work, or would you like to offer 30-day terms? Maybe you want to offer 30-day terms with a discount if the invoice is paid in full within 10 or 15 days.

Some people really don't think about when they want to be paid. Consider the importance of this question,

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though—when will receiving that money benefit you and your company *the most*? It might be right before your bills are due so that you have the cash on hand to pay them on time. Maybe you even want to pay them early to take advantage of early pay discounts—thus saving yourself even more money. No matter what you decide upon for terms, choose a time of the month that you want to be paid—the first of each month, the 15th, or any date that works best for your business—and stick with it when setting your due dates.

Now, take a moment to picture yourself in the following scenario. You are sitting at your desk and a customer that you had great confidence would pay you is past-due and avoiding you. The balance is quite large, and the debt is getting older and older. What do you want to happen when your customer is late or doesn't pay you? Do you want their credit to be revoked? Their account to go on hold for future orders until this is paid? A phone call to be made or a letter to be sent?

Once you have a past-due customer or a bad check, you can take the following steps when customers are past-due, over their credit limit, or bouncing checks.

- Refer to your Credit Policy.
- Make a collection phone call.
- Send a friendly (or not so friendly) reminder.
- Revoke credit.
- Stay on top of your accounts receivables and follow up with anyone you contact.

If you are still having trouble with an account, go back to the sales department and talk to whoever made the sale. Sales will have gathered information on what the customer

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can and cannot afford; do not oversell! When an account is past-due, have the sales person who made the sale contact the customer.

The least popular method in getting the sales department to help collect is to withhold commissions on sales until customers have paid for the item in full.

It is absolutely vital for you to take these steps *before* your business is in a cash flow crisis. Make sure you have all of your credit-approved customers' accounts up-to-date and paid off in full. Take steps now to resolve any issues if anyone is past-due. Review all your credit-approved customers and make sure you have a current and up-to-date credit application, as well as a credit limit that works well for both them and you. Watch customers who may be in danger of losing their jobs or their homes, because chances are that they will not be able to pay you if this happens.

The following list of "Top 10 ways to avoid bad debt" is comprised of things you can start doing right now. Even if you just try one new thing a week, at least you are doing *something* that will help you maintain control of your cash flow.

1. Stay on top of balances owed.
2. Contact a customer immediately if they start to get overdue.
3. Do not continue to ship products to a customer who is not paying on time.
4. Reevaluate credit limits once a year.
5. Get a signed credit application from every customer.
6. Check references.
7. Stay firm!
8. Follow up.

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9. Send invoices immediately after products are shipped or service is performed.
10. Fire customers who are not profitable.

According to psychologists, up to 90 percent of human behavior is habitual. If you have a habit of letting your receivables get overdue—a fairly common unsuccessful habit—you will always get a predictable result. Negative habits breed negative consequences, so you want to choose a better, more successful habit to replace this one. Three steps you can take to change this habit are to:

1. Review your accounts receivables weekly or, at the very least, monthly.
2. Stay motivated by trying to collect as much money as possible.
3. Stay focused; don't allow customer excuses to get you off track.

Once you have these habits in place, keeping your receivables up to date will be your new habit—one that will make you more money and grow your business.

The following is a recap of the best steps you can take to help you achieve success with your credit policies.

1. *Get more information than the P.O. box number.* To increase your collection agency's chances of tracking down an individual or business, always ask for the customer's physical address, phone number, and Social Security number. All of this information will be helpful in finding individuals, even if they have closed their P.O. box or changed their address and phone number. This

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information helps the agency do a better job in collecting for you.

2. *Check credit and get a signed Credit Application*. Fend off collections problems from the very beginning by running credit checks on new clients and by discussing your prices, service fees, and payment requirements with new customers before you do any work for them. Carefully check credit references of each new account and don't extend more credit than the business can handle.
3. *Explain transaction terms thoroughly*. When extending credit, make sure that accounts know when you expect payment, and clearly detail any credits or penalties for early or late payment.
4. *Follow up overdue accounts*. Always be prompt when sending statements and reminders of payment due dates. Make phone calls if necessary.
5. *Institute a series of overdue notices*. Schedule regular written and oral reminders before you even consider using a collection agency.
6. *Set an absolute due date—and stick to it*. As a final step, establish a firm due date before you turn the account over to a collection agency. Do not extend this date, but do give the debtor warning of it. Once this date has passed with no payment, then you can place the account with a collection agency with the knowledge that your customer has been properly notified.

REMEMBER

Make your customer aware of the terms when you make the sale or at the time of the order. Customers are usually happy

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to comply if they see your stated credit terms right from the beginning.

Make your reminder friendly at first; many businesses pay 90 to 120 days after purchase. You can send a notice to speed up payment via e-mail or fax; both are effective ways to touch base with a slow paying customer.

Next, make a phone call. You should always assume payment has been made and ask "When did you send your check?" Then don't say anything. Let the customer break the silence no matter how long or uncomfortable it may seem.

Finally, pick up the payment in person. Once you show up in person to pick up a payment, you should never have to do this again—that is, if the customer has every intention of paying. If, however, you repeatedly have to visit their place of business, you may want to put them on a COD basis.

WHAT *NOT* TO DO

- Don't tell your friends at the monthly Chamber meeting that the customer is a deadbeat.
- Don't plaster online bulletin boards or mailing lists with notes telling the world that your customer is a bad credit risk.
- Don't hang copies of the bad checks around town or in your place of business.

Doing things like this can get you sued. You can also get yourself into legal hot water by making threats, using harassing or abusive language, making collection calls at odd hours or too often, or by making false statements about what

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will happen if the debtor doesn't pay. Creditors need to be aware of the FDCPA even though they are not required by law to follow it unless the state laws specify that they mirror or follow the FDCPA.