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DIVA'S NEW VENTURE

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> It pays to remember that what we are actually doing every time we work without being paid up front is, in effect, lending to our customers"

WHEN CUSTOMERS WON'T PAY

How to avoid dealing with business who don't pay, and what you can do when they refuse to.

BY COLIN PORTER

Non-payers, defaulters, fly-by-nighters. It's a sad fact of business that if you deal with customers on credit terms, you're likely to have encountered the type of customer who – when the work is done or the product delivered – refuses to pay.

Most of us have a horror story about a client who consumed time, resources and cash before dodging their debt – sometimes declaring that they couldn't settle, other times simply going missing.

When considering this problem, it's worth remembering why we sell on credit terms in the first place. We do so because it's part of our *service*, because it distinguishes us from competitors who won't. In other words, it's a courtesy. It doesn't have to be extended in every case, and it pays to remember that what we are actually doing every time we work without being paid up-front is, in effect, *lending* to our customers. With that in mind, here are some things you can do to deal with customers who won't pay.

1. AVOID THEM

This is the most effective way to deal with non-payers. Unfortunately, they don't identify themselves up front. A common practice is to ask new customers for trade references, but this is flawed because customers are unlikely to give you the details of a company they haven't paid.

Instead, make sure that you investigate the credit record of the customer in question. Start by doing an ASIC search (asic.gov.au) to check the company's particulars. Then check the company's credit history with a credit registry such as CreditorWatch, or Corporate Scorecard. The bigger the job, the more research you should do. If you do find something adverse, it's up to you whether you're going to deal with them on more stringent terms or not at all.

2. HAVE POLICIES AND PROCEDURES

If you were a bank lending money, you'd put procedures in place to assess your customers and chase their debts. In business, things should be no different:

- Make sure that you have written policies in place that govern when credit can be extended, on what terms, and how it will be pursued when overdue.
- Get new customers to complete an account application form that details your terms and policies. This helps to set expectations.
- Send reminders at 30 days and 45 days, or whenever is appropriate for your industry and your kind of business.

- Set a limit, such as 90 days overdue, when you will begin to take further action.
- Get a lawyer to help you to draft a final notice informing customers that their debt must be paid immediately to avoid legal action and the registering of a default.

Having procedures to follow helps to 'train' your clients about your practices while showing them that you take credit seriously. In addition, businesses who don't follow up usually get paid last, so having credit measures in place will often get your business paid ahead of someone else.

3. CHASE THE DEBT

The golden rule of payment collection is that the squeaky wheel gets the grease. Make sure that your business *actively* pursues overdue debts. This can be by letter or telephone (try both) and – if you think it's worth your time – you can even attempt to collect in person.

When a customer won't pay, try to understand why. Do they have a cashflow problem, or are they close to collapse? If they claim cashflow, ask them to pay in instalments. Be sure however that any agreement struck outlines a precise payment schedule and contains penalties (such as immediate legal action and the registering of a default) for a missed payment.

A common reason customers cite for non-payment is that the products and services delivered weren't what they expected. While this can be a ploy, try to discuss any issues raised in good faith. You may need to offer compensation or a discount, which – though not ideal – will at least mean that your business recovers something.

DEALING WITH BAD DEBTORS

- Perform credit checks on new customers.
- Get customers to complete credit application forms.
- Have processes for actively chasing debts and sending out reminders.
- Specify consequences for missed payments. Report defaults to rwegistries like CreditorWatch.
- Outsource to a debt collector if you can't chase yourself.
- Take legal action only if you're likely to succeed.

4. CONSIDER A DEBT COLLECTOR

While debt collectors don't do anything that you couldn't do yourself, they are more practiced and may have more success in chasing your recalcitrant debtor.

Their usual practice is to work for a percentage of the debt recovered, and using one can be a good idea if your business doesn't have the in-house staff it needs to chase debts on its own.

Keep in mind however that debt collectors don't have additional legal powers, and if they are overzealous you may damage your relations with a customer by using them.

5. REPORT A DEFAULT

If a business refuses to pay you after 90 days, you should let other businesses know by reporting the default to credit monitoring organisations. While this might not help you to collect your particular debt, the threat of such action can often compel a customer to pay.

Also, while in the past the sharing of credit data has been the domain of large companies and financial institutions, new services aimed at SMEs are now appearing on the scene. CreditorWatch, for example, is a new online community of business owners who share information about debtors in order to be instantly alerted when the businesses around them cause payment trouble. Users of the service also place a logo on their invoices to encourage on-time payment.

6. TAKE LEGAL ACTION

When all else fails, it's time to consider court action. Unfortunately, this is never a quick or inexpensive solution. Indeed, it can take 18 months or more for the process to complete, and most of anything you recover can be chewed up by legal costs.

Most jurisdictions in Australia have a Small Claims Court or Tribunal – often attached to the magistrates court – in which you can make claims. While it's cheaper to lodge in such forums, their actions are not usually enforceable. Local and magistrates courts will provide enforceable judgements, but their rulings aren't automatically enforced. You will need to request action from the sheriff's office, which can run into difficulties trying to identify seizable assets.

The upshot is that unless the debt that you're pursing is large and you also know that the company in question has the ability to pay, legal action may be more trouble than it's worth. In all cases, the best thing to do is consult a lawyer.

One advantage of legal proceedings is that their initiation can often bring about mediation and negotiation. If you don't get the debt back, remember that depending on your tax situation you can usually 'write it off'.

CHANGING TIMES

The situation in Australia is that payments are taking longer and longer. In part, this is a product of the GFC, when cashflows were tight. Now however, with the economy in recovery, some businesses are likely to use these lax payment terms as a tool for building their own cash reserves – meaning that we should be more stringent and aggressive in pursing debts.

As the economy picks up, our natural inclination is also to take on as much new business as we can find. But it's important not to do this at the expense of proper debt management and careful consideration of each customer. Remember that you might have a great and profitable business with great products and still be undone by unpaid debts or by customers going under. DB

—Colin Porter is the founder of CreditorWatch.com.au, a new registry where businesses share information about bad debtors to make better credit decisions.

> ONLINE

www.creditorwatch.com.au