

# Protect Your Bottom Line: Plan and Implement a Successful Collections Policy

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July 17, 2013



Sticking to a sound collections policy is important, but many small businesses do not give sufficient attention to this component of their trade. With proper planning, some losses can be avoided. Ignoring the need for a collections policy may affect your bottom line.

Debt collection. It's an activity as old as money itself. Just hearing those words can stir up thoughts of harassing phone calls, threatening letters, and other horror stories involving unsavory individuals who make a habit of acting outside of the law, or, at the very least, thoughts of uncomfortable personal interactions and severed relationships. From this, it is easy to see how you and your business might prefer to focus on other aspects of your operations, devoting little or no time to the development and implementation of a collections policy. Nevertheless, despite the negative connotations of debt collection, your business can and should cultivate and enforce a reasonable collections policy to protect your profitability.

## What Is A Collections Policy?

A collections policy is a defined procedure followed by a business to ensure that its customers pay their accounts on a timely basis. Collections policies can vary by trade, industry, and business, and, in some instances, by customer accounts. The policy can be formal or informal, rigid or flexible, written or unwritten. There is no one size fits all to developing and implementing a collections policy. However, there are general actions that every business, including yours, can take to proactively minimize losses on its past-due accounts.

## Do You Have The Proper Documentation?

Ensuring that your business has the proper credit documentation is the first step in the process. Credit documentation can include credit applications, financial statements, credit agreements, promissory notes, guaranty agreements, monthly billing statements, and invoices. Ask potential customers for business references, and follow up with the references provided. These items establish the relationship between your business and your customers, the existence of the debt owed by your customers, and your rights and remedies in the event your customer fails to pay your bill. The documentation may help you decide whether or not to extend your goods or services on credit to a particular customer, thus avoiding a problem account up-front and "encouraging" customers to pay your bill before they pay others, and then, if they don't pay, proving your claim to a court if all else fails. All types of credit documentation may not be applicable to your business. Select or have documents prepared for you that best apply to your business model and integrate their use into your daily operations.

If you already have credit documentation in place, it may be beneficial to have it reviewed again. Do not rely on outdated agreements. Your business environment is fluid and changing, and you should make every effort to ensure that your business protections keep up as well. Do your credit documents appropriately address your current business needs? Do your agreements still comply with all relevant laws? Are there new or enhanced protections that could be included in your documentation?

## **How Well Do You Know Your Customer?**

Is your customer an individual person or a business entity? Do you know your customer's actual and complete legal name? Is it a limited liability company, corporation, partnership, limited partnership, or different type of business entity? If it is a corporation, for example, does its name end in "Corporation," "Corp.," "Co.," or "Inc.?" The distinction is legally significant, but you'd be surprised how many corporations use the wrong term in their day-to-day business affairs and operations! Does the customer operate under a trade name? The more you know about your customer, the better you will be able to protect your bottom line. If possible, take the time to get to know your customers and their businesses. Remember – knowledge is power.

## **What Can You Do To Protect Your Business?**

Be diligent and proactive. Monitor your accounts receivable on a regular basis. Invoice your customers for the sums they owe on a monthly or even more frequent basis. Include a provision in your credit documentation that allows you to collect reasonable attorneys' fees if necessary. This can make a difference in your ability to negotiate with your customer and whether it is worthwhile to pursue a claim in court. Charge interest or late fees on past due accounts. If a customer falls behind on your bills, reach out sooner rather than later. Send a reminder invoice with a late fee added, if applicable. Pick up the telephone and make a call to the customer. Keeping regular and professional contact with your customer will go a long way toward reducing past due accounts.

In some instances, you may be able to withhold or stop the delivery of goods sold on credit, reclaim goods that have already been delivered, refuse to provide further goods or services to a non-paying customer, or cancel your contract with that customer. You may also be able to renegotiate the terms of your contract to impose shorter payment terms, require advance payment by the customer for your goods or services, or require the customer to provide security for your account. The remedies available to you will vary on a case-by-case basis and may be dictated by the terms of your credit documentation.

## **Going To Court**

Lawsuits are expensive and should be avoided if at all possible. However, if all else fails, a civil claim may be your only recourse. While the customer may have no current funds to pay its account with you or the judgment you might obtain in court, the good thing about a court-imposed judgment is that it is a lien on all real property of the customer in each county where the judgment is filed for at least ten years (20 years if you decide to renew it), and often the customer will be required to pay your judgment years after you have obtained it (plus the legal rate of interest) in order to sell any of its real property or enter into future transactions with other parties.

Of course, some accounts will be so small that it would just not make economic sense to sue for collection. However, two recent changes in North Carolina law can help you and make it worthwhile for you to pursue additional court actions.

First, § 6-21.6 of the North Carolina General Statutes has been amended to allow for the collection of attorneys' fees based on contractual agreements, but only if the attorneys' fees provision is "reciprocal" – that is, equally applicable to all parties. An example of such a provision is that the losing party, whichever party that is, can be ordered to pay the prevailing party's "reasonable" attorneys' fees. This is one big reason your credit documentation is so important: Good documentation will increase your chances of being the prevailing party and thus getting reimbursement for your reasonable attorneys' fees if your documentation correctly provides for such fees to be paid.

Second, the jurisdiction of Small Claims Court has been increased to include matters not exceeding \$10,000.00 in amount. The great thing about Small Claims Court is that it is much more informal than the District and Superior Courts, and many parties represent themselves without having to pay for attorneys and all the formal pleading required in District and Superior Courts. And if your credit documentation is in good order, you may be able to win just by presentation of your documentation.

## **Conclusion**

The development and implementation of a collections policy should be a priority matter for your business. Document your credit relationships, know your customers, and be diligent and proactive in your efforts to collect accounts. It is up to you to find a policy that works best for your business and stick to it. After all, no one is in a better position than you to look out for your own best interests.

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