HOW TO RECOVER AFTER A CLIENT DOESN'T PAY

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Suffering a non-payment event—whether it's your first, the most recent, or the most significant—can feel overwhelming. Damage to companies is never solved overnight. Restoring optimism and trust is an ongoing challenge.

Non-payments can actually add up and damage your company on multiple fronts. Even ignoring a relatively-small invoice can hurt your bottom line—especially if you depend on receiving a payment in time to pay expenses or if you rely disproportionately on a small number of clients, AKA "concentration risk."

So what do you do when a customer doesn't pay? Knowing where to start is essential.

WHERE TO START

1 CONTACT THE CUSTOMER

The first logical step is to make contact with the customer. Sometimes a phone call or resending the invoice is enough to secure payment. If this doesn't work, explain the consequences of nonpayment in a courteous way—whether it's discontinuing their service or reporting their delinquency to a credit-rating organization if the payment is not received in the agreed timeframe.

2 CALL A COLLECTION AGENCY

If contacting the customer is not successful, you may consider calling a collection agency. This way, you task another company with collecting the payment, and you free up your staff's time for other work. This may be the best solution for small payments, and you often won't have to put up any money—the collection agency takes a part of the recovered sum. For larger delinquent payments, filing a lawsuit may be warranted. Talk to your attorney about how to proceed in your state; you may not need representation for the proceedings, but it is a good idea to get legal advice before filing a suit.

3 PAY ATTENTION TO YOUR STAFF

Make sure to pay attention to your staff. In severe non-payment events, your cash flow may be damaged, and employee morale may be impacted, especially if you have to introduce job cuts and other cost-saving measures to remain competitive. In these cases, it benefits you to foster open and honest two-way communication between employees and management about the situation, what is being done to resolve it, and how it will be avoided moving forward. Maintain trust by making sure that payroll is satisfied and that employees have clear expectations about when they will receive their checks. If you have to get a bridge loan or pursue financing to ensure these payments, do so. If your employees stop trusting you, you could end up facing even bigger issues, like non-attendance and loss of reputation.

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HOW TO AVOID NON-PAYMENTS FROM THE START

A customer non-payment event is typically the first time many customers look into their loss-mitigation options. You might find that you simply don't have the time or the resources to pursue the issue in court or through a collections agency, especially if the amount is small. Additionally, these options can be of limited use if the non-payment was a result of an insolvency or formal bankruptcy.

Going forward, it helps to understand a little more about how the non-payment occurred in the first place:

- Did you have systems in place to prevent loss or limit your exposure?
- Did you get contracts signed?
- Did you outline your deliverables and payment terms?

You can make nonpayment less likely to happen by answering these questions and being proactive. You can then begin to mitigate your A/R risk by following the best practices described below:

1 START WITH THE BASICS

A basic place to start is to make sure that invoices are sent out regularly by adhering to a repeatable process. Also take steps to address non-payment the minute that a receivable becomes overdue. Sending notices of late invoices helps highlight the issue, and the practice provides a valuable paper trail so that you are prepared if you need to escalate the matter later. Also make sure that the employee overseeing your A/R is aware of how to pursue the issue—in court or via a collection agency. To this end, you will want to ensure that all parties involved understand the legal rights afforded by your location and any statutory limitations to which your company may be vulnerable. Remember that in the case of a smaller claim, you may be able to represent yourself in small claims court and avoid the cost of legal representation.

2 STANDARDIZE BUSINESS PRACTICES

After you've been burned by a non-payment event, start the rebuilding process by establishing a predictable standard for your core A/R business practices. Remember that in order to collect on a receivable, you will need to generate documentation supporting your claim.

Every time you work with a customer, create a contract that specifies the work or products you provide as well as the payment schedule to which your customer has agreed. Write out the time line and spell out the consequences of late payments. If you have not already done so, consider hiring an attorney to draft your company's standard terms and conditions. These conditions should specify the customer's agreement to cover all costs related to debt collection—including but not

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HOW TO AVOID NON-PAYMENTS FROM THE START (CONTINUED)

limited to third-party collection expenses, late fees, and legal fees. As part of your standardized process going forward, require customers to agree to these terms when applying for credit terms with your company.

3 IMPLEMENT NEW POLICIES

If non-payment has been a real issue for your company, you may also want to institute new policies to protect yourself. Many companies use down payments, cash-up-front terms, retainers, or milestone payments to minimize the amounts they could lose. Another option could be to keep an alternative form of payment on file such as a credit card, and include in your agreement a remedy to charge the account in the case of a missed invoice.

Establishing a clear, signed agreement is key for an option like this. While these options insulate you from some or all of the receivables risk, keep in mind that they may also impact your competitive edge; if your competitors offer open terms and you require cash terms, you may lose business.

4 CREDIT MONITORING

Your credit team's primary responsibility is to check and monitor the creditworthiness of your prospective and existing customers. Creditworthiness is fluid, so this is not a "one-and-done" task. Rather, you should implement a defined system of monitoring for changes in financial health, particularly warning signs of distress. This process should be informed of the relative risk of customers, with more frequent checks for newer, smaller and less-stable companies.

Also officially document your credit policies and procedures to define how creditworthiness is determined and monitored. This document should specify data sources including (but not limited to) bank and trade references, credit reports, individual company financial statements, and ongoing monitoring of political risk and macroeconomic risk.

Prudent credit management is a tough and never-ending job; you may want to consider augmenting your internal staff by partnering with capable experts to ensure efficiency and thoroughness.

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5 PROTECT YOUR RECEIVABLES

In addition, consider credit insurance, also known as accounts receivable insurance. Like other types of insurance that protect your assets from unexpected loss, credit insurance protects against a loss in your largest and most vulnerable asset—your A/R.

However, the commonalities between credit insurance and other insurance end there. A credit insurance policy with a world-leading carrier is more like a partnership with a worldwide network of risk-management experts. The carrier provides data and insights to help you pick the right customers to do business with, monitors their financial health throughout the year, and reimburses you in the event a covered customer fails to pay.

REGAIN YOUR PEACE-OF-MIND

It isn't easy to bounce back from the disruption that can be caused by an unexpected non-payment event, especially if there is significant operational and morale damage left in its wake. However, remember that you survived it in the end and are now able to treat it as a wake-up call—taking steps to better prepare your company for these events in the future.

As you start to take on the challenge, setting up predictable policies and procedures that incorporate industry best practices can be step one. As a powerful step two, consider engaging with a partner like Euler Hermes, who is in the business of information and risk management. This kind of relationship helps you make sure the next non-payment doesn't impact your company's solvency.

Even companies who have never been burned by a significant loss may find they are limiting their growth potential by being overly conservative with their credit risks. This tendency is magnified by companies who have been stung by a non-payment. The investment in a credit insurance policy can often pay for itself multiple times over—even if a claim is never filed, simply by fueling safe, but aggressive sales in the future.

For more information on how to help your business avoid non-payments and mitigate A/R risk, contact Euler Hermes at www.eulerhermes.us.