BizSkills

Transcript of Webinar recorded on 18/5/17
14 Things You Can Do to Reduce the Risk of a Customer Not Paying

Title Slide

Hello everyone and thank you for joining the webinar this afternoon. I am running this webinar without an assistant so let's hope nothing goes amiss. If you have any questions, you can write them in the message box and I will answer them at the end of my presentation. Then, after the webinar, if all goes well, I will send you a recording of the session plus a transcript of my notes. So, let's begin.

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My name is Zanette Phillips and my business is called Biz Skills. My background has been in office administration, and in business management for over 30 years, covering 20 different industries. Many of the businesses I worked for had debtor's ledgers and I have always had a good customer debt collection rate, regardless of the type industry.

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I established Biz Skills because I saw a need to develop a better way to collect customer debt in a systematic and strategic manner rather than the ad hoc and unplanned methods that many businesses are using. These methods are obviously not working, otherwise so many businesses would not be closing their doors due to unpaid customer debt. There are formal courses available for accounts personnel to learn the basics of processing accounts receivable, but little, if any, of this training is about how to control all the facets of customer debt for small business. And of the training that is available, very little of the advice can be easily translated or implemented into an office system. Many people learn on the job from other employees. And often small business owners employ bookkeepers assuming that they will be able to collect customer debt successfully, but the fact is, most people hate phoning customers about outstanding debt. Quite often, the reason they hate the job is they feel they could be facing a confrontational situation with some of the customers.

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My business and website is online lecture courses that focus on teaching business owners and accounts people to control customer debt by being proactive rather than reactive.

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To define reactive. Basically, debt collection for business is the reaction of a business owner to a customer not paying what is owed by the date the payment of the invoice is due. And that reaction is debt collection activities such as phoning, reminders, debt collection letters and legal action.
Being proactive is to establish upfront processes such as strategies and policies and procedures so you can train your customers to pay their invoices on time, and thereby reduce the need for debt collection activities. Also, being proactive means

you are in control of the system and thereby reduce the risk of confrontation. Debt collection will never be an enjoyable job but setting up your system to be proactive means you will reduce your stress levels and put your time to better use in such activities as marketing for increased sales. There are many ways to reduce the risk of customers not paying and today I will give you 14 of them.

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Initially, you need to take a proactive approach when giving your customers credit and the longer an invoice is outstanding, the harder it is to collect and there is no point in making a sale if you don't get paid for it.

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The first thing you can do is

1. Give customers no more credit than your business can afford. If you cannot afford to give 30 days' then only give 14 days or try to get cash as much as possible. A business owner needs to ask themselves - can their business afford to finance a debtor's ledger? For those who don't know what financing a debtor's ledger is – if your customers are not paying you, and you do not have sufficient funds coming into your business to pay your wages and overheads, then you will need to find other means to pay for those costs. And that may be a business loan or overdraft -, or a credit card, if loans are not available. Whatever the finance facility it will cost the business in interest. Another issue the business owner needs to consider is how much time it takes to manage a debtor's ledger. Is the business owner trying to run a business and do the accounts themselves? How much time do they wish to spend on this process? Is the business employing part time staff to process the accounts? Do the office staff have time to collect debts plus other duties. These are important issues as the less time spent on collecting outstanding customer debt could mean a delay in getting the payments on time and the risk of non-payment increases. Maybe the business should place tighter restrictions on who get credit so less invoices are outstanding and less time is spent on managing the debtor's ledger. Businesses that can cause some strain on your ledger are large corporations and generally, you cannot dictate your terms of trade to them, unless you can come to a special agreement. The bigger companies receive many invoices, and do not have the time to process individual payments for small businesses according to their terms. In saying that, if your invoice is processed without any problems, you are probably going to see your payment on time after 30 days or in whatever terms they pay. If you deal with a company who pays in 60 to 90 days, which some international companies do, you will need to determine if you can afford to carry the debt for that period of time; particularly if you have had to trim your price to get the sale.

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The next is

2. Don't give credit by default – if they don't ask for it, don't give it. If you delay in invoicing a one-off sale because of time restraints, you may not get paid at all. Many businesses give credit to customers by default because they have difficulty in negotiating with their customers; are not organised; they do not have a credit

management plan and are late sending out invoices. There are many business people who get so excited to make a sale that they extend credit to anyone who walks through the door or calls to place an order. Other business owners will extend credit to a new customer without getting the customers last name and there are also businesses that do not ensure their salespeople get quality customers – the ones who can pay. It's not the sale that should be the target but the paid sale. A sale that is not paid, costs the business money and may in turn close its doors.

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3. Don't give 'one-off sale' customers credit. They will not be motivated to pay, if they are not going to buy from you again. There is no strategy you can use, such as cutting off their credit, or advising legal action will happen if they don't pay. Because these will have little effect, - especially if the invoice is small, and you are not likely to take it any further. Therefore, writing off the sale will be your only option. I would like to relate a case study to you to illustrate the problem of giving one-off sale customers credit. I was employed to manage a glass and aluminium fabrication business in a regional town about 15 years ago. When I took over the job there was a problem with non-commercial customers in particular not paying for the repairs of broken windows or doors. Most of the problems were occurring with transient housing tenants who were engaging the business to fix their windows so they could get their rent bond back and leave town. The business was not collecting the payment after the job was done and sent out an invoice a few days later. Needless to say, the tenant was long gone and so was the money. I set up a credit policy that no non-commercial customers would receive credit and they were advised upfront, when the order for the job to be done was placed, that they had to pay the tradesman before he left the premises, in cash – no cheques.

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4. Be alert for customers who have no intentions of paying in the first place. There does not seem to be enough discussion about this issue even though everyone has seen a story on TV about rip-offs to customers, but the same thing occurs to small business owners every day. We hear about situations of the general public trying to get something for nothing, but it happens with small businesses ripping-off other small businesses. I would like to relate another case study to illustrate this. A plumber agreed to do a job for a hairdresser and quoted the job for about $5,000. The hairdresser was a small business and they were sent a progress claim about halfway through the job. The plumber told them he wanted to be paid before he went any further. They said they would have all the money by Friday and he believed them. Friday came and the plumber presented them with the balance invoice and then he was told that they had no money. It was then established, they did not have any money before they engaged him for the job. The plumber was placed in the position of having to pay for all the fittings and labour used on the job as he had taken on this job in good faith as most tradespeople do. No, the plumber did not write this off. Instead he set them up on a payment plan and received the money at $150 per week. An arduous task,

but he got it all. He could have avoided all the stress of this situation by asking the customer for a deposit up front, at least to cover the purchase of the fittings. If they could not pay that, he could have asked himself, if he would have been paid at the end of the job. So, he could have given himself the option of stepping away from the job. You need to assess your customer carefully – especially the 'payment on completion' jobs where you get paid after the job or service has been done.

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5. Ask for a deposit before buying appliances or equipment, particularly if the goods are non-returnable or need to be paid by COD. On a job where the purchase of equipment or hire of labour is required, you should consider asking for a deposit to at least cover that purchase, or you are putting yourself at risk. Asking for a deposit to cover the items you have to finance up front is not unreasonable, and if the customer refuses then you could ask yourself, are you going to get the payment for the whole invoice after the job is finished. I have another case study to relate to you as an example of this situation. An electrician was given a job to install an air conditioner of some value. The electrician bought the air-conditioner and then the customer changed his mind and cancelled the job leaving the electrician holding the air-conditioner which was not returnable. Unfortunately, the money was not recovered. Be careful taking on the purchase of expensive equipment in the hope that your customer will have integrity. In this case, the electrician could have asked for a deposit that covered the retail cost of the air-conditioner before buying the equipment, and then negotiated his terms of trade on the installation. Alternately the electrician could have asked the customer to buy the air-conditioner and just charged for the installation.

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6. Give all customers who ask for credit an application and assess it thoroughly for creditworthiness. That also means phoning the referees. In numbers 2 and 3 of this list I advise not to give credit to on-off sale customers and not to give credit by default. All customers who are not cash sales should be given a credit application and the form should be filled out by the customer completely without crossing sections out because it suits them. You cannot apply for a loan to a bank and get away with crossing parts out so why should your business be different. The bottom line is credit is credit whether it is from a bank or from your business. Biggest difference is the bank earns interest from the credit it provides whereas your business does not. Therefore, the credit you give to a customer costs your business and most people do not know how much that cost equates to. Believe me, quite a lot. I cover the cost of running a debtor's ledger in two of my ledger management courses. Going back to the application. Many businesses do request customers fill out credit applications, but the forms just end up being customer details collection forms and often the referees are not checked out. Or the customer gives a referee who will not take phone calls or give a reference. In this instance, the business should go back to the customer and ask for a more compliant referee. Some people say, customers will only give their best or favourite referee. But consider this – if the referee is a business, are they going to

lie? **Their** reputation could be at risk if they give an untrustworthy person a good recommendation.

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7. Don't just rely on a credit agency report. Some businesses use this service as their only source of credit reporting. Many small businesses do not report defaults to the agencies – they just write the sale off. Hence the report will be insufficient and not give you a complete picture of the customer's trading history with other businesses. A credit agency is not going to tell you how prompt your prospective customers pay suppliers, the credit limits other businesses have given, the volume of purchases and whether they can be considered a creditworthy customer for any business that will deal with them. Only a referee can answer these sorts of questions and more if you think any. And, you should be using a prepared questionnaire so all referees are asked the same set of probing questions. Enough questions to satisfy you that your prospective customer is worth taking the risk to give credit to.

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Once you have assessed your customer carefully and accepted their application, you should send them a letter of approval, detailing the terms of trade you are offering, their credit limit and the consequences that will occur if they exceed the terms you have offered, such as stopping credit if invoices are not paid by due date and the credit limit is exceeded. It is important to follow through with these rules otherwise the customer is not going to take you seriously. It would help if you had a Customer Credit Policy prepared, that establishes who you will provide credit to, what restrictions you will place on the customer you provide credit to, such as credit limits or shorter terms until they prove themselves creditworthy. What assurances you need from the customer to give them an ongoing account, and who will give the authorisation to accept a new customer for a credit account.

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8. Follow an Overdue Invoice Strategy and train your customers to pay by due date. An overdue invoice strategy is designed to make sure your customers pay their outstanding invoices on time and you are alerted to any problems your customers may have with their cash flow. An important component of the process to make the strategy work efficiently, is advising your customers of your Terms of trade upfront at the point of sale, or when you issue the quote. This means you have a greater capacity to request the payment when you want to be paid. For instance, if you advise a customer upfront that you want to be paid in seven days and confirm the customer's agreement that they understand those terms, then when you phone, because they have not paid in 7 days, you can confidently remind them of the agreement they made with your business. If you have that agreement signed for, it is even better as you can send them a copy showing their signature. The overall plan of the strategy consists of when you will make the first phone call and when you will send reminders. Reminders should only support or reinforce the phone calls, not be in place of the personal contact. Accounting

software companies are trying to sell their products by saying you will be paid quicker with their amazing automatic reminders that will save you time, and you will get paid 2 times faster. Don't believe the hype. No-one pays because they get an automatic reminder. The overdue customer knows they owe you money and some will do anything to avoid paying. The strategy also includes when to send out the strong letters leading to legal action. Hence it is worth putting the strategy in place so you have a plan and a process

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9. Phone within a couple of days after invoice due date to identify customers with cash flow problems. If you phone 3 days after the payment should have been made, then you will identify if your customer is having financial difficulties and you will be able to take action depending on what those difficulties are. You may want to place the customer on stop credit as you could be **increasing their** debt and **decreasing** your chances of being paid. You may want to offer to supply by COD, so the customer's business can continue trading if their difficulty is short term. In the meantime, the current debt can be paid off at an amount negotiated, so that the original debt is being reduced. Sometimes a customer might ask why you are calling so soon after the due date. After all it only 3 days. You can reply, that you gave the customer 30 days' credit, not 33 days, so you want to be paid now. Many people lack confidence or feel uncomfortable about phoning for outstanding debt. A phone script may assist you in having questions to ask and other information so you can investigate further about why your invoice was not paid by due date. My courses explain how to deal with various customer excuses and there are many. Some are valid, such as the customer may require a proof of delivery before they pay. Some mining companies require this if you have sent a piece of equipment to a remote site and having the documents confirming delivery from a freight company would probably be the requirement. Some excuses are not acceptable, such as 'when we get paid, you will get paid'. The phone script is included in the ledger management courses, but I have prepared a separate course, just dealing with the phone script, for those who are interested, and it also includes dealing with customer excuses and delinquents debtors.

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10. Place a customer with cash flow problems on stop credit, don't make the problem any worse for you or the customer. If a customer is avoiding paying <u>you</u> because **their** customers are avoiding paying <u>them</u>, then you do not want to add to their debt. Because if one of <u>their</u> customers goes into bankruptcy, that in turn could affect the financial viability of <u>your</u> customer. Adding to a customer's debt by supplying more goods is not going to help you. Yes, you will have more sales but what is the point of extra sales if they are not paid for. In addition, you might realise the customer has a problem, with only one month's invoices outstanding, for which you could negotiate a payment agreement to pay off the debt. But if you continue to supply more goods, the debt you have to negotiate will get larger and hence create more work for you. Your risk of non-payment will increase substantially every time you supply more goods and the longer the debt remains

outstanding. One of the problems people forget, is that while you are waiting to be paid for your outstanding invoices, you will have to pay your suppliers for any goods that were used on the job. You could risk losing your suppliers account if you don't pay them. So, in essence you are financing your customer. And if the customer does not pay at all, then the goods that you have paid for to do the job, will in fact be donated to the customer. Especially if the goods were installed in the customer's premises.

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11. Make sure the customer is advised, understands and acknowledges your terms of trade before you open an account for them. To illustrate this situation, I would like to relate a case study where a new customer was not advised the terms of trade of the business – actually he was not assessed properly in the first place. I was working for a mining supplies company, in a rural town some years ago. My manager gave an earthmoving customer 60 days' credit, and $50,000 worth of goods, based on the fact he looked like a 'nice guy, and he had lots of earthmoving machinery' – in other words – he looked like he had plenty of money. I phoned the customers office before the 60 days' due date, to ask when they were scheduling our payment. The accounts person would not discuss the issue, advising we had given them 60 days' credit. I phoned again at 60 days and could not get past the receptionist. They went into receivership a week later. Don't be fooled by appearances. When the manager opened the account for this customer no terms of trade were agreed upon and no referees were asked for. He just relied on his personal assessment and judgement of people to make a decision that the customer was creditworthy and gave 60 days to pay. And who wouldn't want a $50,000 sale. Some business people get so excited about getting a sale – particularly a large one, that they do not want to think that the customer may not have the money to pay for it.

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12. Constantly monitor credit account customers for cash flow problems. Just because they were creditworthy when the account was opened does not mean they won't have a problem in the future. There is more to the story I told you about in the previous item. In this case, the customer was not assessed for creditworthiness in the first place, but he may have been at the time of the initial negotiation. And because the manager gave 60 days to pay - something may have occurred in the meantime to change his financial situation. Maybe the customer lost a large contract he was counting on. As it happened, the person who owned the earthmoving business had several companies, and he sold the equipment from one company to another, to leave the company we were dealing with, a mountain of debt. This situation resulted in a huge court case. And the company I was working for wrote the sale off. The customer had used the goods sold to him, so he got them for nothing. What should have happened in this situation was that the customer should have been given a credit application, and asked to provide some referees which could have highlighted some cash flow problems. A limit on how much he could purchase until he proved himself creditworthy, and no more than 30 days' terms. Everyone in the business should

have been mindful of the company policies that new customers are properly assessed before the account is opened. This sort of situation becomes a debt collection nightmare.

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13. Follow up overdue accounts consistently, preferably weekly. Being consistent in all the aspects of controlling customer debt is important to reduce the risk of non-payment of customer's invoices. You cannot expect to be paid if you do not put proper procedures in place. Many employees do not like debt collecting and will make excuses that they do not have time to do the task. A debtor's ledger is an asset and is the equivalent of cash in the bank. It is money that just has not managed to get into the bank because your customers have not paid. Hence it demands the same amount of respect and attention as any other asset. If your business has a fleet of vehicles you would not be lax about having them maintained because you do not have time. You know that there are consequences of not maintaining vehicles and it can be expensive. So that your debtor's ledger can be maintained properly, the answer is strong policies and procedures with the goal of reducing the risk of non-payment of customer debt and reducing the costs of running the ledger. Most business people do not know how much their ledger is costing them to run and the longer the debt is outstanding the higher the cost. If you go to my website and click on courses, then click on the debtor's ledger management course details you will find a 5-minute video explaining how to reduce your ledger balance by 50%. The video also explains how much you will save by changing the way you manage your ledger. Training your employees to focus on getting the paid sale rather than just reaching a sales target will increase your profitability because you will not have those extra costs. I explain in both my ledger management courses how much it is costing and the amount may surprise you.

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14. Set up a proactive Debtor's Ledger Management system to control customer debt. Most people think the debtor's ledger is just about accounts receivable, but if you want to reduce debt collecting activities and receive payments on time, then, the process is much more than that. I have incorporated all the elements of controlling customer debt into one integrated system. The elements are: accounts receivable, customer negotiation, customer credit assessment, policies and procedures, debt collection activities, training employees and cash flow management. The system looks at improving office procedures and setting up strategies to reduce the current customer debt and then manage the future customer debt with an overdue invoice strategy.

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I have also written specific policies and procedures to support the elements which are the customer credit policy, the terms of trade policy and the complaints policy. Plus, the debtor's ledger management policy which refers to the previous three policies and includes the overdue invoice strategy. There is another policy I have prepared which is the credit policy and management plan. This policy is to monitor

and protect your cash flow. If you can't manage the cash and credit that flows through your business, it will inevitably fail.
To give an idea how much your ledger is costing your business.

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A ledger of about $300,000 that has debts outstanding 60 and 90 days, can cost a business around $2,000 a month in interest from a credit facility to pay the bills, plus unearned interest because the customer payments are not in the bank. In addition, the labour costs of chasing the outstanding debt and the cost of writing off sales. Often people do not consider the amount of sales to be generated just to break even after a write off. To give you an example, if a small business wrote off one sale for $5,000, and were getting 5% net profit, they would have to generate $95,000 in sales to break even. So that would be a total of $100,000 in sales with no profit to show for their effort just because one person did not pay their account. Since most people go into business to make money, these costs sound like a good reason to put a more efficient system in place for your business.

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I would like to give you some targets. If you are invoicing 30-day terms and collecting some cash sales, then you should not be carrying any more than one month's average sales at month end close off, and all should be collected by 45 days. There should be nothing outstanding in 60 days. If you are invoicing 7-day terms then you should be carrying no more than two weeks' average sales. If the 7-day invoices are chased at the end of the month, then you will probably be carrying 5 to 6 weeks' average sales or more. The danger in this situation is, if a customer cannot pay, then you will be adding to the problem by providing more goods and services and not addressing the cash flow problem. The consequence is that you may not get paid at all.

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If you would like more information about managing your ledger, controlling customer debt and other associated issues, you can read my blog page on the Biz Skills Website and sign up. I generally prepare a blog for the website and an article to LinkedIn at least once a week.

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And to find out how healthy your debtor's ledger system is, you can download a FREE office procedures assessment questionnaire from Biz Skills website to identify the gaps in your system. Don't return the questionnaire for a score as no two businesses are alike. The document is designed to stimulate your thinking so you can evaluate what sort of system you would like in your business.

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To learn more about proactively training your customer to pay by due date, Biz Skills **Debtor's Ledger Management** and **Effective Debt Collection Strategies** online lecture courses include strategies to reduce the current customer debt, to collect future overdue invoices and to train your customer to pay their invoices by due date.

You will also find a step by step guide to create a Complaints Policy and a course called Responding to Customer Complaints which is the communication skills for a front-line person who does not have the authority to resolve complaints but needs to preserve the customer relationship during the complaints process.

If anyone has any questions please submit them and I will see if I can answer them.

So, if that is all the questions for today I will conclude this webinar and if anyone wishes to contact me you will find my contact details on my website.

www.bizskills.com.au