

Increase Successful Debt Collections: A Guide for Business Owners



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A Guide for Business Owners



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Tips to Increase Successful Debt Collections



Introduction

As a Pennsylvania collections attorney, I have encountered many obstacles that prohibit successful collections throughout the years. Common issues include the debtor filing for bankruptcy, the debtor having no assets, the debtor cannot be located or the cost to proceed with collection efforts is too high when compared to the amount of the debt. While some of these issues cannot be prevented, some due diligence on the part of the creditor at various times can increase the ability to collect from a debtor.

Establish a Universal Payment Policy

One of the many issues I see as a collections attorney is a business' poor handling of accounts receivables. As a business owner, you need to establish a meaningful, strict process for handling accounts receivables. All businesses should have a procedure that includes timely invoicing to clients and customers, timely follow up (usually every 30 days), form letters to send after 30, 60 and 90 days of non-payment, and a process for handling delinquent accounts over 90 days that may include the use of a collections attorney.

Once you have invoiced your customer according to your payment policy, but the invoice remains unpaid, be sure to remind your late-paying customer of your payment policy and that they owe you money. If you don't remind your customers that they owe you

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money, you most likely will not get paid. Sometimes clients simply forget about payment obligations. With a well-established universal payment policy, the likelihood of absentminded payment errors decreases substantially.



If a customer ignores your regular invoice, contact the customer directly. Try placing a reminder call or visiting the customer in person. It is important to remain polite and professional and to practice good customer service. Your tone should be one of concern. Ask your customer if they are having trouble making the payment, and then work together to come up with solutions, such as an installment plan.

The longer a debt remains unpaid, the greater the chance of never receiving payment for that debt. If a debt remains unpaid, the debtor could fall further into financial distress and other creditors can enter the picture. Debtors can file for bankruptcy protection, relocate, sell valuable assets or redirect payment to other creditors, all at the peril of the business that is not quick to act or at is not at least proactive in its handling of accounts receivables. Having a simple concrete process in place can make all the difference.

Practice Due Diligence Prior to Entering Contracts

Businesses often have very little recourse against a debtor customer when the debtor customer becomes insolvent, files for bankruptcy or becomes inactive. A debtor in these cases usually has no assets to pay the debt or satisfy a judgment. Many times, these situations can be avoided with some due diligence before entering into a business relationship with the customer.

Some due diligence strategies include a credit check, a judgment and lien search in a county index, asset search, UCC search and requests for financials including tax returns, profit and loss statements and other asset and liability information. It is also useful to obtain information and references from other vendors, suppliers and customers of the business to gain valuable insight into the company's integrity and respect for payment on invoices. All of this is easy to accumulate and tells a story about the financial viability of the company. The information will help the business creditor make sound decisions when entering into a business relationship with a potential customer to lessen the risk of unpaid invoices.

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Use Written Contracts

I cannot overstate the importance of using written contracts for your business transactions. Make this your policy with every new client. Even if the use of written contracts is not common practice in your industry, use them anyway. Sensible clients will recognize that you need the terms of your business relationship in writing to protect your business.

Your contract must include key terms, including a description of the product or service to be provided, when you will provide it, and the terms of payment required of the customer. You should enlist the assistance of an experienced business lawyer to help you draft your contracts. There are template contracts available online and elsewhere, but these one-size-fits-all forms generally fail to include many provisions necessary to provide ample protection to business owners in case of default.



Forum Selection Clause

One specific and useful tool for creditors to consider is the inclusion of a Forum Selection Clause as part of a written contract. A Forum Selection Clause allows the parties to agree that any litigation arising from the contract will be commenced in a specific forum. For example, a Texas company that has a customer in Pennsylvania that defaults on a payment obligation may have to start a lawsuit in Pennsylvania without this clause. The cost to travel and proceed with the lawsuit may force the Texas company to abandon collection efforts. With a Forum Selection Clause that establishes Texas as the proper forum for litigation, the Texas company can proceed with a lawsuit in Texas, obtain a judgment, if necessary, and then transfer the judgment to Pennsylvania for enforcement and collection. Commencing a lawsuit in the home state of the creditor often forces the debtor to pay or settle the matter because it is too costly and time consuming for the debtor to engage in litigation outside of its home state.

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Attorney Fees Clause

As stated above, a written contract is always strongly recommended. Another important feature of a written contract is an attorney fees clause. An attorney fees clause requires the losing party in litigation to reimburse the prevailing party for its attorney fees and costs. If a business sues a customer for breach of contract for the customer's failure to pay and the business prevails, the customer will be responsible for payment of the original debt plus the business' attorney fees and costs to litigate the matter.

This is important for obvious reasons. First, it decreases the financial risk to the business creditor for having to pursue litigation. Second, it increases the financial risk to the debtor and may cause the debtor to rethink a strategy that may include delaying payment by tying up the matter in court. Third, it helps to facilitate a settlement and quicker payment.



The Importance of a Personal Guarantor

Most business owners set up a corporation or limited liability company (LLC) because the corporation or LLC shields its owners from personal liability on any debts or obligations of the company. In other words, a business debt is usually not the personal responsibility of the owner, even though the company may have a single owner. Business creditors must take caution when entering into contracts or agreements with any business because the business will be responsible for the debt and not the individuals who own the business. Entering into a business arrangement with a start up company with very little income and assets can be risky. Other risky arrangements include businesses that have poor credit ratings, owe money to various creditors, or have poor cash flow.

Business creditors should always consider having an individual owner of a business guaranty payment or performance under the contract. This is known as a personal

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guaranty. Let's say, for example, that you are a commercial real estate business and you want to lease office space to a start up company. The start up company signs a three year lease; however, after only four months, the start up company fails and closes its doors. The start up company still owes you money for rent. You can attempt to sue to enforce the lease and collect payments; however, an insolvent company cannot pay even if you obtain a judgment. Alternatively, if you had the owner of the start up company sign a personal guaranty from the outset, the guaranty document will provide for recourse against the individual (guarantor) if the company fails to make its payment obligation. The individual may have money or other assets that can be used to satisfy the debt which will increase your ability to collect payment.

A personal guaranty should always be considered. It provides a business creditor with another avenue for collecting payment.

Be Flexible

The more forms of payment your business accepts, the more likely it is that you will receive timely payment from your customers. If you don't already, consider accepting major credit cards, which may give your customer the ability to pay your entire invoice at once. Remember, however, that a fraction of each credit card transaction must be paid to the credit card company. Other payment arrangements you might want to consider are installment payments, retainer deposits for professional services, prompt-pay discounts, PayPal or other online forms of payment.

You should also try to be flexible regarding potential settlements from delinquent customers. Business owners are sometimes hesitant to accept settlement offers because the business owner feels entitled to the full amount owed. While this sentiment is understandable, it is important to remember that if a client is struggling financially, there is always the possibility of a bankruptcy filing, which will often preclude you from collecting anything.

Formal Demand Letter

Statistically, if you haven't received payment after ninety (90) days, your client is probably not going to pay you willingly. At this point, after you have made repeated attempts to contact your customer to no avail, it may be time to consider pursuing more aggressive collection strategies, such as a formal demand letter.

You should have your attorney draft a formal demand letter on your behalf because there are federal guidelines that must be abided by as a debt collector. Your attorney should be an experienced commercial collections attorney who is licensed to practice law in the state where the debtor is located. A formal demand letter should include a description of the products or services provided, the date(s) of service, a demand for the total amount owed, instructions for payment, a concrete deadline for payment and specific consequences

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of nonpayment. The letter should be sent via Certified U.S. Mail with a Return Receipt requested and should include any referenced invoices, etc. as enclosures.

Mechanics' Lien

A mechanics' lien is a legal tool available to contractors and subcontractors that can prove useful as a mechanism for getting paid. A mechanics' lien places a hold on the title to real property so that the property cannot be sold without the owner first paying the contractor for work performed. Each state has its own mechanics' lien law. Pennsylvania's lien law, the PA Mechanics' Lien Law of 1963, provides descriptions of the types of improvements and property for which mechanics' liens can be used as well as timelines and limitations for filing and perfecting the lien. Mechanics' liens are extremely time-sensitive and must contain many specific provisions governed by statute. Further, the practice and procedure to obtain judgment on a claim filed is governed by the Pennsylvania Rules of Civil Procedure. For these reasons, it is often best to utilize the services of an attorney for the filing and perfecting of a mechanics' lien claim.

Use a Good Collections Attorney

If you cannot collect the debt yourself, you may want to outsource the problem to a debt collection professional. There are two (2) types of debt collection professionals: collection agencies and collection attorneys. Third-party collection agencies generally employ the same strategies you have already attempted – writing letters and placing phone calls to the debtor. Collection agencies are notorious for abrasive debt collection practices, so it may not be in your best interest to utilize one to collect a debt from someone whose future business you may value.

Alternatively, a collections attorney can draft a formal demand letter, file a lawsuit, obtain a judgment and attach assets, or negotiate a settlement agreement with a debtor. A good collections attorney is responsive, aggressive and experienced in commercial debt collections, with access to superior resources for locating assets such as bank accounts. A good collections attorney should also suggest a fair fee agreement for the debt collection, offering contingency, hourly or a combination fee arrangement. Collections attorneys typically charge less than collection agencies by utilizing these types of arrangements.

About the Author

Jason B. Martin, Esq. is a Pennsylvania collections attorney and the founder of the Martin Law Firm, P.C., located in Blue Bell, Montgomery County, PA. As a commercial debt collections law firm, the Martin Law Firm assists businesses nationwide with debt collection actions throughout Pennsylvania and New Jersey. To learn more about how a commercial collections attorney can help your business, please visit our [commercial collections website](http://www.jbmartinlaw.com).

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