

When you keep your side of the bargain with a customer, it is only fair that they should keep theirs by paying you... and paying you on time. Sadly, as everyone in business knows, this doesn't always happen.

How big is the problem?

The bad debt calculator below shows you how many extra sales you will have to make in order to recoup the profit you lose on a single bad debt. For example, if your profit margin is 10%, and a £5000 invoice is not paid, then you will have to make another £50,000 worth of good sales to make up the profit lost on the one bad sale. Shocking, isn't it?

Your profit margin %	Bad debts					
	£100	£1000	£5000	£10,000	£50,000	£100,000
1%	£10,000	£100,000	£500,000	£1 million	£5 million	£10 million
3%	£3,333	£33,333	£166,666	£333,333	£1.7 million	£3.3 million
5%	£2,000	£20,000	£100,000	£200,000	£1 million	£2 million
10%	£1,000	£10,000	£50,000	£100,000	£500,000	£1 million
15%	£666	£6,666	£33,333	£66,666	£333,333	£666,666
20%	£500	£5,000	£25,000	£50,000	£250,000	£500,000
30%	£333	£3,333	£16,666	£33,333	£166,666	£333,333
40%	£250	£2,500	£12,500	£25,000	£125,000	£250,000
50%	£200	£2,000	£10,000	£20,000	£100,000	£200,000

Why does it happen?

In their 1999 survey, business finance specialists Alex Lawrie asked UK companies why they paid invoices late. The top ten reasons given by credit controllers were as follows:

- 23% Waiting for the cheques to be signed
- 22% Invoice lost
- 16% Cashflow problems
- 15% Person dealing with it is unavailable or off sick
- 6% Cheque is in the post
- 5% Waiting for the cheque run or for a new cheque book
- 3% The invoice is being disputed
- 2% We pay on 60/90 days – not 30 days
- 2% Missed the payment run

On a lighter note, some of the more bizarre reasons given by credit controllers when refusing to pay included:

- “The owner has been buried with his cheque book”
- “All names are put in a hat. If yours is drawn out you get paid. If not it stays in the hat for next month”
- “I do not speak English”
- “We're in the middle of an armed robbery”
- “Not now, its the office party”
- “The tide is out and the owner is unable to get in to pay cheques”

What can you do about it? Some unusual ideas that really work....

- 1 **Prize draw** – One business supplier in the North East holds a monthly prize draw. Every customer who has paid their account on time goes into the hat, and once a month a winner is drawn out and treated to a meal for two at the best restaurant in town. The scheme costs about £1200 a year to run. And not only does it greatly improve cashflow, but it also creates a talking point and makes customers smile.
- 2 **Big prompt payment discounts** – Most prompt payment discounts don't work because the 1%-5% discount traditionally offered is not enough to galvanise customers into action. So a Leeds based business we work with gives its customers a massive 33% settlement discount. But just look at how it does it.... its main product has a list price of £3000, which it is usually prepared to discount down to £2000. But rather than make that £1000 reduction a "sales discount", it makes it a "prompt payment discount".

In other words, the invoice shows the price as £3000, but also contains a line that deducts the £1000 and reads: "This £1000 prompt payment discount may only be deducted if payment is received at our office no later than..." followed by a date exactly 7 days from the invoice date. As a result the vast majority of customers pay within 7 days. Why not turn your sales discounts into BIG prompt payment discounts in this way?

- 3 **Increase you prices** – Another business we know wrote to all its customers telling them that that it was increasing all of its prices by one ninth (ie 11.11%). But in the same letter it also explained that customers paying within 14 days of the invoice date would be able to deduct 10% from the invoice value. Nobody complained, and most of its customers now pay within 14 days. What's more, and here's the amazing part, customers now actually come in to say "thank you" for being allowed to pay less by paying early!

Of course, when you look at the maths you see how clever this particular strategy is. Initially a £100 item goes up to £111.11. So those who pay after 14 days pay the full £111.11. While those who pay within 14 days pay £111.11 less the £11.11 prompt payment discount – which comes back to the £100 they used to pay before the price rise. So either the business gets paid *more* or it gets paid *more quickly* – and either way its owners are happy!

- 4 **Prompt payment benefits** – Discounts are not the only way you can motivate and reward customers for paying you promptly. There are many other benefits that you could reserve only for those who pay on time. For example, you could give them priority when booking service and repair visits, free upgrades to express delivery, or even free delivery, lower minimum order quantities, extra technical support, free helpline, special offers on upgrades, discounts on their next purchase, access to a special section of your website, extended warranty terms, membership of a user group, advance notice of new products or whatever else is most relevant in your case. The key is to make these benefits exclusive to customers who pay on time, because that way many more of your customers *will* pay on time.
- 5 **Prompt payment club** – Taking the last idea one step further, why not bundle all those exclusive benefits as part of a prompt payment club – which customers are automatically members of if they pay on time. And perhaps give it a name like "Integrity" – since that helps all your customers to see that, when they demonstrate high integrity by paying you on time, they will get special privileges. It will also help them to realise that by paying late they are acting without integrity.
- 6 **Payment upfront** – Another powerful approach is to insist on payment upfront. A useful way of explaining this is to say: "In order to ensure that we have sufficient

resources available to continually improve the level of service you receive, our policy is not to ask our good clients to subsidise the handful of clients who abuse credit terms by not paying promptly (and, in some cases, not paying at all!). As a result our standard terms are that payment is due when we start the work.”

- 7 **Offer finance** – Some retailers (car dealers and white goods retailers in particular) offer to arrange finance for their customers. But most others don't. And that is all the more strange considering that finance allows the business owner to make more sales (because more people will be able to afford to buy), get paid quickly, and perhaps even share in the profits made by the finance company. There are now many specialist finance companies offering many different types of finance options. For example many professionals now offer their clients the opportunity to pay in instalments by signing a simple agreement with a finance company – and because it is what is know as “recourse financing”, there are no processing delays, very low rates of interest, and the finance company guarantees never to turn down an application. Why not explore whether you can arrange something similar for your customers?
- 8 **Using humour** – Humour is a great way to defuse difficult situations – including asking to be paid. Some businesses use funny cartoon postcards and faxes to chase debtors. Other use amusing letters. For example, the text given below (which works best as an e-mail, but can also be used as a letter) gets extremely good reactions and results.

Dear Fred

My name is BRIAN and I'm the Bloggins & Co computer.

I've got some good news, some really good news and some even better news for you.

The good news is that, at the moment, only you and I know that your invoice for £XX (ref: XX, date) is overdue.

The really good news is that I am not programmed to tell [insert partner's name] about it for another seven days.

And the even better news is that I've discovered a way for us to sort it out between ourselves without involving him.

All you need to is send me cheque in the next seven days and I will erase the overdue record from my hard drive. That way no-one else need ever know.

Yours etc

BRIAN

Finally, don't forget to ask us for a copy of our “Getting paid checklist” – since it contains 43 extra ideas to help you collect every single penny you are owed.

Disclaimer:

The information in this document is of a general nature and is not a substitute for professional advice. You are recommended to obtain specific professional advice before you take any action. © Copyright 2001 Added Value Solutions. All Rights Reserved.

Getting paid checklist

Nos	Question	Yes	No	Action where answer is "No"
1	New customers			
1.1	Do you have a standard credit enquiry form – and is it used for every new customer?			
1.2	Do you always get full contact details?			
1.3	Do you always take up trade references?			
1.4	Do you always get bank references?			
1.5	Do you always do a credit check?			
1.6	Do you always set a credit limit?			
1.7	Are credit terms always agreed in writing?			
1.8	Do you always use your own standard (and expertly written) terms of trade?			
1.9	Do you use a credit monitoring service for major customers to give you advance notice of any changes in their credit worthiness?			
2	Orders			
2.1	Do you always get a written order from the customer?			
2.2	Do you always make sure that the order form small print doesn't attempt to change any of the previously agreed terms of business? <i>NB: This is known as "The battle of the forms"</i>			
2.3	Where the small print on the order form does differ from the agreed terms, do you make sure that the differences are resolved in writing before accepting the order?			
2.4	Do you always check whether the order will take the customer over their credit limit – and refuse to take orders that do?			
2.5	Do you always get and keep proof of delivery?			
2.6	Do you always make sure that the details on your delivery note are accurate?			
3	Invoicing			
3.1	Do every single one of your invoices include ALL of the following details: <ul style="list-style-type: none"> ■ Customer name and address ■ Address to which payment should be sent ■ Terms and conditions ■ Purchase order details - name, number and date ■ Description of items supplied ■ Quantity details ■ Price details and discounts given ■ VAT rates, calculations and totals ■ Your VAT number ■ Total amount due ■ Date payment is due by ■ Payment terms 			
3.2	Are invoices raised the day goods are delivered?			

3.3	Are invoices sent on the day they are raised?			
3.4	Do you double check that the delivery is of the right thing, in the right quantity, to the right place and at the right time... in order to avoid invoice disputes?			
3.5	Are all invoices double checked for accuracy before being sent?			
3.6	When sending large invoices do you always confirm that they have been received?			
4	Collecting			
4.1	Do you always have an accurate and up to date aged debtors listing to refer to?			
4.2	Do you phone customers before large invoices are due to make sure there are no disputes?			
4.3	Do you always chase overdue debts within 7 days of them becoming overdue?			
4.4	Do you chase the largest overdue debts first?			
4.5	Do you have a set of letters and telephone scripts that get progressively firmer as the debt gets older and older?			
4.6	Are they used every single time?			
4.7	Do you have a clear policy on when to use a solicitor or debt collection agency?			
4.8	Do you always pursue claims through to the courts where necessary?			
4.9	Do you have a system for resolving delivery and invoice disputes quickly?			
4.10	Do you keep a log of all "explanations" that can be referred back to quickly before each stage of the debtor chasing process?			
4.11	Do you send statements every 14 days?			
4.12	Do you bring the non-payment of an invoice to the attention of the actual user as well as the accounts department?			
4.13	Do you hold a monthly prize draw for prompt payers?			
4.14	Do you offer large settlement discounts?			
4.15	Have you thought about putting your prices up by one-ninth, but offering a 10% discount to customer who pay within 14 days?			
4.16	Have you created a bundle of other benefits exclusively for prompt paying customers?			
4.17	Do you ask for payment in advance?			
4.18	Do you use humour to help you chase debts?			
5	Other			
5.1	Do you use factoring and invoice discounting?			
5.2	Do you report to senior management the debtor days, amount of overdue debt, and the percentage of total debts that they represent?			
5.3	Do you accept credit cards?			
5.4	Do you arrange external finance for customers?			