20 Collection Tips You Must Do Now

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ABO'S TOP 20 COLLECTION TIPS YOU MUST DO NOW

(Sung to "*Show me The Money*")

*"WORDS PAY NO DEBTS" (*William Shakespeare)

"WHY *LEAVE YOUR MONEY IN SOMEONE ELSE'S POCKET?" (*Martin Abo, CPA)

"*THANKS FOR THE INFORMATION, CAPTAIN OBVIOUS" (*Benjamin Abo)

Of the three quotes from above, the last one from my son Benjamin, may be the most appropriate for those reading the thoughts that follow about managing a firm's accounts receivable. We all feel we know what to do - we just need to so remind ourselves and, as per the Nike ad we need to…."JUST DO IT".

As most business people know, the more past due your receivables become, the less likely that you'll collect what is owed. For manufacturers, retailers, lawyers, doctors, distributors, and accountants – you name the business or profession – a while ago a commercial collection firm provided me some insight on the collectability of past due accounts as they age which I believe still holds true. Here is the data:

Amount of Time Past Due	Average Recovery Rate
30 days	97%
90 days	90%
120 days	80%
180 days	67%
1 year	45%
2 years	23%
3 years	12%

The figures clearly reveal the decline in value with the age of past due accounts, and they certainly support the need for firm and aggressive collection efforts in any organization. If your collections are deteriorating, you might want to discuss the situation with your accountant (hopefully us), an attorney seasoned in this arena (assuming you're not) and a collection consultant in order to examine your practices and recommend modifications. I'm a CPA and, as such, we typically refer to customers as "clients" and billings as "fees". The same holds true for lawyers or other consultants. Doctors may refer to patients and fees. Retailers, distributors, manufacturers may sell product rather than services and call them customers and consider them as just plain sales. Pardon my interchanging of the terms or displaying my bias from my world of accounting firms and law firm but the underlying theme is the same….It's your money…Go Get It!

That said; consider the 20 thoughts that follow but, certainly, in no particular order of priority.

1. Bill responsively from the outset. Issue invoices as soon as feasible, preferably coincident to the providing of the service. Delaying can lengthen the payment period. In addition, frequently the more credit you extend, the more you must borrow. Shortening the billing cycle while speeding up your collection process can have a profound impact on distributable income to the firm's owners/partners. For example, while every business is unique, with service professionals no different, the average law firm may have 80 days of unbilled work while it typically takes another 60 days to collect those fees even after they've been invoiced. You add it up - 140 days from the time the services are performed until the payment is deposited and fully available to the firm. That's almost 5 months. If you can cut that "delay" by just a third, you could free up enough cash for a partner distribution of one and a half months worth of fees!

   The cost of extending credit is a good example of the hidden costs that "eat up" working capital. Just ask your accountant to show you the math. Consider the cost in direct bad debt losses as well as in payroll dollars for the time, effort and attention that slow paying accounts cost your firm. These are the truly hidden costs for these efforts and the least enjoyable part of any job (Abo considers it akin to "combat pay"). Then add the cost of capital tied up in receivables to the interest you pay to carry such receivables.

   I've seen some pro-active companies having a pleasant-voiced administrative person call the client after 10 to 15 days of closing a matter and the billing. The call, effectively a well disguised "customer service" or "public relations" follow-up, is an excellent time to so remind the client of their payment responsibilities (diplomatically, of course).

   Speeding up billing has a ripple effect in reducing related problems and ultimate write-offs or *adjustments (i.e. payment for services performed almost 5 months after when actual payroll was incurred; monies could have been available earlier but were used for other "squeaky wheel vendors"; providers will often make concessions when time has passed; client appreciation has already waned with the passage of time, etc.). On a similar note, pay attention to inadvertent delays by the professional(s) involved in completion of the matter. Since often you may not be able to final bill before the client receives some final document/notification/follow-up, do not let such files sit on your desk, your associate's desk or even your secretary's desk.

2. Where permissible, consider requiring:
   a. Advance Payments
   b. Evergreen deposit
   c. Payment by credit card
   d. Installment payment agreement
   e. Automatic debit memo on bank account
   f. A standby letter of credit guaranteeing the payment
   g. Personal guarantees from the client (or even a third party)
   h. Obtaining a pledge of assets from the client
   i. Having the client pay at least the current invoices on a current basis.
   j. The application of any excess payment against past due invoices.

k. A C.O.D. or advance payments with respect to new services.
l. Payment of outstanding invoices before starting new matters.
m. Consider utilizing a bank lockbox to accelerate collections and cash flow. This is particularly effective when a number of clients are concentrated at locations quite distant from your office.

3. Try stating on each invoice sent out the discount for prompt payment **<u>in dollars</u>**, not merely as a percentage such as "2/10 net 30". Also focus on the actual design of your invoice. If the invoice is confusing and doesn't clearly identify the services rendered, the costs incurred, or the terms of payment, it is quite possible that the recipients may delay payment until the appropriate operating personnel can verify what was performed and that payment can be made. Similarly, if the address and other details as to where the payment is to be directed and what documentation is to be enclosed are unclear, delays can occur at either end of the transaction before payment is made or can be deposited.

   Discounts work for many of our manufacturing or distribution clients so why shouldn't they apply to professional service firms? If you do offer payment discounts and would like to accelerate collections and improve both public relations and cash flow, consider <u>writing clients</u> who don't take discounts simply because they wish to delay their payment. Point out to them by taking the discounts and paying sooner, they can enhance their own financial performance. Assuming you provide typical terms of "2/10, net 30", your letter might make the following points:

   1. By not utilizing the discount, the customer is borrowing from your firm;
   2. Based upon your terms, by delaying payment for the additional 20 days, the cost to the customer is increased $2 for every $100 owed;
   3. On an annualized basis, the cost of not taking this discount is equivalent to an interest charge of **37.23%**
   4. There are undoubtedly considerably less costly ways to borrow;
   5. The amount of discounts lost, based on the total amount of annual fees could have enabled the client to obtain additional services or products without cost.

   Your clients will appreciate this information and you may encourage increased cash flow from your accounts receivable. Incidentally, these facts equally apply to your own accounts payable if you're not taking advantage of discounts from vendors.

   Your offering such cash discounts may actually bring collections in at less cost. For example, if offering the "2/10, net 30" cash discount provides prompt payment incentives for a client to pay within 10 days rather than his or her normal 60 days, the financing costs to your firm would be 14.4% (i.e. 360 days divided by 50 days times 2%). Again, it works for other commercial enterprises, so why not for service professionals like us? Of course, if most of your clients were prompt payers, establishing a cash discount policy to provide an incentive for the remaining few wouldn't be cost effective. The firm may prefer to just stop doing business with the slow paying clients. I should state here that an alternative approach for dealing with slow paying clients is to add an interest surcharge for payments received after the 30^{th} day.

4. Who says billing has to take place right after the end of the month? Establish the billing period to end one to five days prior to the billing frequency you've established. For example, if you were billing for the calendar month September, consider billing from August 25th through September 24th. Receipt of these bills from the firm may better match when businesses and individuals alike pay their bills. Please realize that many business and individual clients pay their bills on a specific day of the month. Payment of invoices that arrive after that date, are put off until their next contemplated payment date, perhaps a month later. Find out what those cut-off dates are for your large clients and make every effort to meet them.

   - Prepare accounts receivable statements at least monthly but do so separate from your actual billing cycle. Also, do not customize cover or status letters to coincide billing. Service firms such as attorneys, accountants or other consultants should send clients a matter update or progress letter separately.
   - Cycle bill by designating specific clients or billing partners to perhaps a 4-week or so billing cycle. Such will spread out the work as well as smooth out the cash flow.
   - Suggest emailing of bills in addition to or sometimes in lieu of mailed paper bills. Make sure the firm tests e-mail addresses and E-bill formats early on.
   - Use window envelopes and include return envelopes with ALL requests for payment (i.e. actual invoices as well as statements).
   - Send the invoice to a "named individual" using first class postage. For very large amounts, consider using courier services.

5. Provide priority processing for large billings and consider requesting progress payments on such large amounts. If your type of firm allows, consider requesting payment in advance or at time of service. Speeding up a few days in receivables can make major cash flow differences.

6. Consider immediately billing the client right after a positive outcome**.** If you invoice when the client is elated because you've negotiated a great settlement or completed a beneficial project, they're more likely to pay and pay quickly.

   But watch out for the "end of the fiscal year squeeze". Especially prevalent in the larger service firms, billing supervisors or partners typically are pressured into putting on the "full court press" in the final days of the firm's year-end. They will often offer their clients significant discounts as many are compensated based on their actual annual collections. Many such clients will not only defer payment awaiting such an offer but also and even worse, begin to expect such discounting throughout the year and on all matters.

7. Large receivables should be pursued more aggressively before telephoning or pursuing smaller accounts. Do not fall prey to merely working in alphabetical or file number order. (<u>And that's not because ABO doesn't want to be your first billing or collection effort</u>). Increase the urgency of second payment requests by use of large lettering, red ink, underscoring, labels, etc.

8. Service firms may want to encourage drifting from the "conventional billing model" to speed up the billing and collection cycle (i.e. agreed upon fixed fees with established progress payments or even payments in advance; monthly or quarterly budgeted advance on an interim basis, etc.). While caution is needed to so monitor profitability, fixed fee arrangements may speed up collection for work performed and enable the firm to benefit from internal efficiencies it gained from technology, similar past projects, leverage of less expensive personnel, etc.

9. Not to downplay the role of the firm's CPA but, honestly, appreciate that most service professionals and small businesses maintain their books on the "cash basis" (at least for tax-reporting purposes and often even in the financial statements they submit to their partners or the bank). Neither accounts receivable (fees billed but uncollected) or work-in-process (unbilled and uncollected fees) may be the focus of attention or even revealed to the reader of the financials. These are often the largest assets of the firm. Such cash basis focus can often mask a receivable problem. One more item, which often is asked of the accountant - cash basis taxpayers cannot deduct bad debts (i.e. uncollectable receivables). If your operating profit margin is, say 10%, than you are going to need additional revenues of $100,000 just to make up a $10,000 accounts receivable loss. Regardless, once you allow a client to lose interest in paying a past due account, as we stated at the beginning of these tips, your chances of ever collecting on that account diminish.

   Here are three methods to use for an up-to-the-minute assessment of your accounts receivable. Sort of an Abo "fiscal check-up":

- **Comparison to your own past experience**. Comparing any given month's receivables with your prior month-to-month figures can tell you when you need to monitor your collection efforts more closely. Try this:

<u>Cash collected during month</u>	<u>$90,000</u>	=	90%
Accounts Receivable on 1st of Month	$100,000		

  If this 90% effectiveness of collections is below the "norm" (average) for prior months, it's time to analyze why.

- **Comparison to your daily fees**. In between too high-pressure collection tactics that alienate clients and too lenient policies that jeopardize your cash flow, there's an optimum turnover of your investment in services provided in credit. That "perfect" receivable turnover period is the shortest period consistent with satisfactory revenue volume and satisfied clients. Want to compute "days" fees outstanding? Try this.

<u>Accounts Receivables</u>	<u>$120,000</u>	=	60 Days Fees
Average Daily Fees	$2,000		Outstanding

  If your terms for service are net 60 days, you may be in fine shape. But if they are net 30, you may have a problem. The above 60 days' fees outstanding calculation is double your current payment terms of 30 days.

- **Comparison to credit sales**. Your annual credit sales in relation to your average monthly receivables can be another important calculation.

<u>Net Annual Credit Services</u>	<u>$710,000</u>	=	6.5
Average Monthly Receivables	$110,000		

  Your turnover is 6.5 times a year, which is pretty good for many businesses. Compare this to your current turnover with standards for law firms (i.e. checking Altman & Weil, Hildebrand, Dun & Bradstreet, etc.) and with your own firm's historical position.

10. For service companies like law, accounting or other consulting enterprises, the engagement letter may be the firm's first line of defense if clients later allege that they were not aware of, or did not agree to, the specific fee structure for the services or the consequences of not meeting their payment obligations. If clients then do not live up to expectations, you will have already communicated the potential ramifications of this. For example, if clients don't pay according to the policies so outlined, you may have stop-work provisions and/or disengagement provisions in the engagement letter that can be enforced. Consider elaborating in your engagement letter how the client will be billed and how the firm expects to be paid

- State how the fee is to be charged, how it will be calculated, when the fee is to be paid and the consequences of non-payment, including your right to withdraw (if ethically permitted). Importantly, spell out the consequences for non-payment within the agreed upon terms.
- State frequency of billing – monthly, bi-monthly or even weekly
- Request a minimum deposit requirement
- Understand whom the firm should contact regarding receipt of invoice and payment. See if a "cc" to or an "information only" party should also be designated. (If the client requires that the invoice be sent to his/her attention, discern the name, number, and e-mail of his/her assistant).
- Remind that client payment does not waive their right to dispute charges later

11. Accept credit cards to make it as easy as possible for clients to pay the firm. Today clients, as well as owners and other employees themselves, live on plastic and, therefore, paying legal, accounting or any other type of bills with credit cards is easy for them. The use of credit cards can be a tool to reduce your receivables and increase your cash flow. Suffice it to say that all credit card companies are not alike. Firms should confer with their accountants and credit card processing consultant to investigate how a particular bank or company charges them.

12. Consider putting a "payment button" on the firm's web site. Many people like paying their bills on line at any hour of the day they're so inclined. By enabling the client to pay through their website, firms can take advantage of this. Payment can be made by either ACH from a bank account or by credit card. Many credit card companies have this service and some have no monthly or additional transaction fees, as do other payment gateways. It isn't necessary to have a "Shopping Cart" to have this capability, nor is it expensive.

13. During less than robust economic times like we are now seeing, client screening becomes a vital process for all companies. You may want to avoid working with clients who appear to have a history of, or are currently experiencing, financial problems; or you may establish different collection methods for these individuals (e.g., collecting retainers, etc.). If applicable, t*ake the time to talk with the predecessor firm regarding the client's payment record.* Remember that past behavior may be the best indicator of future performance. In any event, some considerations before accepting a new client are:

    a. Make sure the customer is ***able*** to pay your price.
    b. Check references (banker, attorney, accountant, insurance agent, etc.).
    c. Contact the predecessor firm and learn as much as you can about why the client defected (or why the predecessor withdrew from the engagement).
    d. Review a Dunn & Bradstreet (or other agency) report on the client's business and ascertain if it is consistent with the financial information you've received.
    e. Make sure the client is ***willing*** to pay your fees.
    f. Discover exactly what this client expects from your firm.
    g. Consider the use of background checks.
    h. I'll say it again: Get a retainer up front, before you begin any services.

Remember*: Think real hard and long if you're even considering a discount on your billing rate or sale price to obtain a client.* Monitor cash flow carefully. One of the first negative effects of a recession is usually found in a slowdown in payment of a firm's accounts receivable. This is the result of your clients using their personal or trade payables as a financing vehicle instead of borrowing from a bank. Making sure that appropriate credit checks are made of all clients and requiring current financial information on all large clients is only prudent in times of tight cash flow. Accounts receivable should be monitored very carefully to ensure that pre-arranged credit terms are being adhered to before new services are provided.

14. For professional service firms, ensure that professionals and para-professionals submit time and expense entries timely and accurately. Errors, even such as misspelling, file number or grammatical, should be avoided. Have the billing people prepare a schedule in advance of dates they will be running bills, contemplating holidays, weekends and even vacations. Assign a manager or partner to ensure such timetables are religiously followed. Prompt review and approval of prebills (draft bills) should be mandated with published turnaround times and performance adhered to. All billing professionals and para-professionals should be held accountable. It may even help to distribute pre-bills on differently colored copy paper so they are readily noticed and segregated from other correspondence, invoices, documents, etc.

    Management should make it clear to all relevant staff that THE FIRM IS IN BUSINESS TO EARN CASH FROM CLIENTS and that A MATTER IS NOT COMPLETE UNTIL IT IS PAID FOR. All professional as well as support staff have a part to play. Partners should be candid with associates and other employees about existing difficulties and about their role and stake in getting the firm though these tough economic times. For example, account queries are not just low-level clerical matters. They are probably complaints from unhappy clients who may feel let down. They justify non-payment and should be resolved ASAP as prime client service priorities.

15. A curious phenomenon is that, when unpaid fees become too large, they often provide an incentive for clients to assert malpractice or product deficiencies in an attempt to avoid or reduce unpaid fee amounts. Such assertions often end up as allegations in a lawsuit. While I may be "preaching to the choir" in presenting this topic to attorneys and other collection professionals, at least appreciate that legal action to collect outstanding professional fees is a common source of professional liability claims (welcome to the club). Fee collection suits following termination of your services are especially problematic. At least recognize that efforts to collect fees, even though they are morally and legally owed you, can result in a counter-suit alleging professional negligence. Re-review the file and always assess potential risks (and costs) of counter-claims when pursuing fee collections against present and former clients.

16. Consider firm-specific practice management software that migrate time and expense entries from emails, appointment calendars, phone calls, expense outlays, etc. directly into invoicing software.

17. Consider making a photocopy of the check from the client, especially if there is a good possibility that the check may bounce and it will likely be retained by the customer's bank. Having made a copy before depositing the check gives you much vital information such as a) the name of the debtor's bank; b) the debtor's bank account number; c) the full name of the debtor; and d) the address appearing on the check, which may differ from the address in your files. All of this information is invaluable if you need to turn the account over for collection or take legal action to collect. Utilize lien rights; bad check laws and other legislative protection to the fullest extent to induce payment. While we as accountants may be of help in implementing suggested procedures and systems, it is incumbent on "legal beagles" to make sure the firm comports within the legal and ethical parameters.

18. It's not uncommon for a client who has run into financial difficulty to make a partial payment of an invoice and write on the check: "Payment in Full." Attorneys can better tell me but I understand that a client cannot make a unilateral accord and satisfaction and force you to accept a reduced payment. Instead, my lay understanding is that the party who presents the check must make clear by conspicuous wording, that the cashing of the check will be construed as a settlement of the outstanding amount owed. Thus, the check or the accompanying payment voucher would have a notation such as*" payment in full of the stated amount*" or "*endorsement of the check constitutes a full settlement of your claim*". This enables you (the recipient) to determine whether to accept the lesser payment or not. Please check the Uniform Commercial Code to confirm the firm, as a vendor, can avoid an accord and satisfaction by returning the money tendered within 90 days. However, I've been told that the mere crossing out of such a restricted endorsement and adding the words "*without prejudice*", and then cashing the check will be deemed an acceptance of an accord and satisfaction that terminates the recipient's right to the amounts still owed. In any event, the mere notation "*Payment in Full*" may not of itself impair a recipient's right to collect the balance of amounts owed.

19. Companies (even law firms) may wish to consider outsourcing the credit and collection function partially or entirely, especially if you have inadequate or inexperienced staff and are unable to proceed with collection efforts on a timely basis. Such collection enterprises typically offer law firms a comprehensive collection service for managing and collecting the firm's accounts receivables, including small claims court service. They may even function as an undisclosed support service in the name of the firm, allowing the firm and the professionals/management to concentrate on sales and operations and not on the running of a collection department or operation. The firm retains this outside agency to handle its accounts collections process, functioning as an extension of the firm, collecting accounts in the name of the firm, effectively operating as the collections back-office.

20. Firms should be aggressive in collecting overdue accounts but don't spend more money chasing small accounts than you can receive by collecting them. Make direct telephone contact quickly with clients who don’t respond satisfactorily to your first dunning letter.

Sample collection letter #1, 15 days late:

Thank you for doing business with our firm. We are appreciative of your business and would hope to continue our excellent business relationship. According to our records, your current balance due is $1,000. Of this amount, $500 is more than 30 days past due. As you know, our normal terms require payment within 30 days after the invoice is sent to you. We know that this is probably an oversight and that you intend to forward the balance immediately. Since you have established an excellent credit rating with us in the past, we are surprised to see a problem arise at this time. If there is some error, or you are unable to pay the amount due immediately, please contact me so that we can correct the situation or make suitable arrangements for prompt payment of this obligation

Please consider this to be a friendly reminder and thank you for your attention to this request.

Very truly yours,
Office Manager

Sample collection letter #2, 30 days later:

We have not received any response from our statements of the last two months nor to our letter of January 10. Your entire account is now 45 days overdue, and you owe us a total of $1,000.

If there is some reason why this payment cannot be made immediately, please contact us so that we can make arrangements that will be mutually agreeable. Perhaps we can work out a payment schedule that would be realistic for your present circumstances.

Naturally, we do not want to endanger your credit rating or destroy the good relationship that we have maintained in the past. Therefore, would you please take care of this obligation immediately so that we will not have to file an unfavorable report with the credit bureau or resort to the use of a collection agency or our collection attorney.

We have enclosed a self-addressed envelope for your convenience. Please return it as soon as possible with your check for the balance owed.

Very truly yours,

Office manager

Sample collection letter #3, 30 days later:

We still have no response from our statements of the past three months or from the letters that we sent you on September 10 and October 10. We are seeking to resolve this matter in a timely and professional manner but we need your cooperation.

Your entire account is now seriously past due: It is obvious that our efforts to clear the account on a mutually agreeable basis have had no impact. Unless we receive payment from you of $1,000 by (date), or can work out a mutually agreeable arrangement to discharge this obligation, we will find it necessary to take further action. This action may include assigning your account to a collection agency. We also reserve the right to initiate binding arbitration to settle this matter as was agreed to by you in the engagement letter, copy attached.

Since this is a costly procedure for both of us, and will cause serious damage to your credit rating, I would suggest that you call immediately so that we can clear the matter at once without resorting to such procedures.

We would regret having to take further action but we will find it necessary if you do not hear from you by [date]. Please send a check for the outstanding amount, or call me today to make arrangements for a payment plan.

Very truly yours,

Office Manager

It is suggested you send the last letter by certified mail ensuring a documented receipt while the client will know this is a serious matter that needs to be acted upon.

If part of the debt is disputed, at least ask the debtor/client to pay the undisputed portion while continuing to resolve the dispute.

21. BONUS TIP

I have a colleague, a collection consultant who is passionate about helping companies, locally and on a national basis, to increase their financial performance by recovering uncollected receivables. Working with a diverse range of clients, he focusing on recovering the most difficult past-due collections and train and improve upon the company's staff and procedures. Anyway, here are 4 types of calls that Robert Leib feels all collection personnel need to master.

a. Soft calls are akin to initial calls to clients who are not presently past-due. Almost has a customer service feel to it.

b. Full payment - Is exactly how it sounds. Full payment is asked for and expected on invoices that are past-due your company's existing terms.

c. Partial payment- at the very least its good practice to request a partial payment on invoices which are past your company's terms- the idea is to get something on the books.

d. Wire transfer- Is always the best form of remittance, its quick and best of all its cash in your bank account.

Always Create a sense of URGENCY in all your customer/client contact via the telephone- Nothing beats a two-way communication with your customer.

If your staff hasn't mastered the above calls for your customer's open invoices, you may be well advised to have them or you confer with such an outside consultant (see my Tip #19 above. As my friend Bob Leib likes to his one tactic as acting as the "wolf in sheep's clothing."

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