

# Credit control

The ACCA logo consists of the letters 'ACCA' in a bold, white, sans-serif font, centered within a solid black square.

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**Credit control is a vital part of running any business — and especially any new business with limited cash resources.**

Every year, thousands of start-up businesses go bust. Many are profitable but are owed money by customers. Unable to pay suppliers, they are eventually forced to cease trading.

This briefing focuses on four key areas.

- Deciding what credit to give a customer.
- Everyday credit control.
- Chasing debts.
- Coping with other companies' bad habits.

## 1 Checking for credit

Is a customer likely to go out of business, leaving you unpaid? Will a customer delay payments, wasting your time as you chase the money? Checking references lets customers know you are serious about credit control.

**1.1** You can now get **online** credit ratings fast enough to use them as a basis for real-time business decisions.

- This can cost as little as £10 to £12.
- Even a highly detailed payment and credit report will not cost more than £35 to £45.
- These ratings can be obtained from credit reference agencies, or through similar services offered by some business support organisations.

**1.2** Ask customers to give you names of suppliers you ask for **trade** references.

Beware of being fed tame suppliers that the customer knows will provide good references.

Ask the referees:

- To confirm your potential customer's trading name and address.
- How long they have dealt with them.
- What credit period they give the customer and whether they get paid on time.
- What credit limit the customer has and how much is currently outstanding.
- Whether they are in any way associated with the customer, other than as an arm's-length trade supplier.

Most references will be given in writing.

Telephone the suppliers to thank them for their help, and ask them if there is anything they can tell you over the phone that they could not put in writing.

**1.3** Another way to check creditworthiness is to apply, with a customer's written permission, for a reference from his or her **bank** (costing about £20 to £25).

- The response will take time and you will need to know how to interpret it, so this may not always be the best option.
- Tell the bank exactly what credit you plan to offer (eg £500 limit, payable monthly).
- Ask if the bank knows of any outstanding writs (demands for payment made through a court).

As a general rule, the longer the reference, the more you should worry.

## 2 Setting credit limits

As a start-up, you may not be able to afford the luxury of only dealing with blue-chip customers. You have to decide how much you are prepared to risk.

**2.1** Set an upper **credit limit** for any customer — an amount you are prepared to risk.

- A customer's credit limit should be based on references and your own checking.

**2.2** If anyone **exceeds** your limit, review the situation carefully. It may indicate problems.

**2.3** Set a **minimum order** size for credit accounts.

**2.4** Do not let **greed** overrule your judgement.

- If a customer wants to buy more than the credit limit allows, get cash for the extra. Otherwise, what seemed like a bumper sale may turn into a bumper bad debt.

### Delving deeper

**A** The larger amount of credit a customer asks for, the more **checks** you must make. As well as checking references, you can:

- Drop in and form your own impressions.
- Ask an agency (eg D&B, 01494 422000) for a credit report.
- Ask your local Business Link, Chamber of Commerce or trade association if it offers a credit-rating service.
- Check the information available to you in your own business. What do your colleagues know about the customer?

**B** Keep up with **events** affecting customers.

- Bad luck, or bad business, can mean a customer who is creditworthy now is close to bankruptcy in six months' time.

**C** If a limited company requests a high credit limit, ask to see their latest **accounts**.

- Or get them from Companies House (0870 333 3636), which cost £5 by email, £9 by post or £12 by fax. Remember, the accounts at Companies House may be 12 to 15 months old.

## 3 Your credit terms

**3.1** Make sure every customer **understands** your credit terms.

- Agree the terms, then ask the customer to sign a copy of the agreement.

**3.2** Set out the **maximum** credit period.

- How many days after the invoice date is payment due?
- Or should the customer pay on a fixed day of each week or month?

**3.3** Have a standard **sales contract** (your lawyer or a trade body can help with the wording).

Consider including such terms as:

- You still own the goods, after delivery to the customer, until they are paid for. Check whether your insurance covers any goods damaged on customers' premises.
- The customer must tell you within a set time if a delivery has not been received. A clause like this helps to avoid disputes.

**3.4** You can offer a **discount** for quick payment to boost cashflow, but always remember to cost this properly (see **Pricing your product or service**).

- Beware of customers who take prompt payment discounts and still pay late.

**3.5** A settlement **rebate** for good payers can often be more effective than discounts.

- You may give regular rebates to customers who have paid on time, based on a percentage of the value of their purchases.

**3.6** Imposing **penalties** for late payment used to be virtually unenforceable. Now it is provided for in law. All businesses can claim interest on late payments, and in many cases, can claim for debt recovery costs.

- Once payment becomes overdue, you may charge interest at the Bank of England base rate plus 8 per cent. The interest must be calculated on a daily basis for each day payment is overdue.
- If you think you may decide to charge interest, tell customers in writing, and draw attention to your right to do so in your terms and conditions. This does not oblige you to collect interest.

“Customers quickly get to know what your attitude is. A reputation for brisk efficiency in chasing up overdue payments is an asset that can help a small business avoid many potential problems.”  
**Andrew Corke, Lester Aldridge Fast Track**

## 4 Everyday credit control

- 4.1 Invoice** promptly. The sooner you invoice, the sooner the payment is due.
- 4.2** Call the customer to **confirm** each delivery has arrived and that no goods were missing or damaged. Confirm the payment details.
- 4.3** Keep unpaid sales invoices in **date order**, so you can see at a glance which ones are the oldest.
- 4.4** Set aside a regular time each week to **chase** outstanding invoices, focusing on:
- The largest debts, followed by the oldest.
  - Customers you guess may have problems.
- 4.5** If a customer exceeds your credit limit, insist the **excess** is paid before accepting any more credit orders.
- 4.6** If a customer has not bought from you for six months, or orders **fall** below your minimum, find out why.
- Is the company going bust?  
If so, try to get any money you are owed as soon as possible.
- 4.7** Every month check the total credit outstanding across your **whole business**.
- How many days' sales does this represent? For example, in a business with sales of £1,000 a day (annual sales of £365,000), total credit outstanding of £44,000 represents 44 days' sales.
  - If the days' sales figure rises, you are being paid more slowly.  
Investigate and correct the problem.

### Warning signs

Your customer may be getting into difficulties if the pattern of payment behaviour changes.

#### A Watch out for **common symptoms**.

- Delays in payment get bigger.
- The customer tries to make payments on account, only paying part of the bill rather than the full amount.

#### B In other cases, the **signs** of trouble may be more clear cut:

- Discounts are taken when not allowed.
- Penalty charges incurred are not paid.

**4.8** In a **seasonal** business you may be unable to chase debts during your busy period.

- Consider making use of a debt collection agency or a specialist solicitor.

## 5 Delayed payments

Customers will often try to delay payment. This may be a danger signal or it may just be because they want to improve their own cashflow at the expense of yours.

**5.1** Call the customer **just before** payment is due to confirm that it will be on time.

**5.2** If a customer makes a **part payment** (payment on account), acknowledge receipt and ask for the balance.

- Negotiate a practical payment scheme (eg post-dated cheques).
- Stop all credit until the debt is paid off.

**5.3** If a customer **queries** one item, insist on full payment for the rest of the order. Sort out the query separately.

**5.4** If a cheque is **incorrect** (unsigned or for the wrong amount), call to point out the error.

- Ask for a new cheque immediately.

**5.5** If a cheque **bounces**, don't jump to conclusions.

- Call the customer, say what has happened and ask how the money will be paid.
- Hold on to the cheque as evidence.

**5.6** Keep records of all the **problems** you have with each customer's payments.

- If customers use delaying tactics, let them know that you know what they are doing.
- Warn customers that they may be put on stop (ie you will supply nothing more to them until the debt is paid).
- Make sure your employees always have access to an up-to-date stop list.

## 6 Chasing debts

The phone is the most effective debt-collection tool of all. If payments are overdue, chase them on the phone. Be firm — but not hostile.

**6.1** Telephone any late payers after a week to ask the **reason** for the delay.

➔ The **Institute of Credit Management** (01780 722900) offers training, consultancy and recruitment services. Meetings at its 26 branches — open to non-members — offer a good learning opportunity.

“Make sure you understand the customer's payment system. Some companies will not pay invoices if you are not established on their payment records or if you do not quote their internal order numbers.”  
**Frank Thaxton,**  
**Thames Valley Partners business advisers**

- Keep a written record of all your calls.
- Send reminders to anyone you do not call.
- If a customer has a fixed or weekly or monthly payment date, call again just before that date.

**6.2 Cultivate** a contact in the accounts-payable office.

- Speak to him or her personally and be thoroughly reasonable, but persistent.

**6.3** If a customer makes an **excuse**, ask when you can expect to be paid.

- Suggest a payment on account and stress that you need cash too to pay your suppliers.
- If cheques are 'in the post', ask customers to check the relevant payment records. Then ask for the cheque numbers.

**6.4** If you **cannot get through** on the phone, try different times of the day.

- Do not accept 'I'll call you back.'
- If the amount is large enough, arrange to call to collect the cheque — and be prepared to wait.

**6.5** If you are still making no progress, consider employing a **debt-collection agency**.

- The commission charged is usually 8 to 10 per cent for commercial debts. Charges for consumer collections vary more, between three per cent and 15 per cent. Unlike solicitors' costs, these charges are not usually reclaimable from the debtor.
- Collection agencies should be registered with the Office of Fair Trading and, ideally, belong to the Credit Services Association.

**6.6** If legal action seems likely, send a **letter of claim**. This begins the legal process.

- The letter says that you plan to sue if overdue bills are not settled by a fixed date (usually 10 days away).
- Write this yourself. You do not need to pay a solicitor to do it.

Unless your debtor is determined to see you in court, the letter will often produce results.

**6.7** After this, you may take **legal action**.

- You may make a small claim at a county court for any amount up to £5,000. You will pay a small fee (£20 to £200) and you should be able to represent yourself. For large claims, seek legal advice.

You have to decide if a debt is worth chasing. The costs involved may make it better to just write off the debt and forget about that customer.

## 7 Working with big companies

Because getting cash in is so urgent for a small business it can be hard to realise how different the culture of larger customers, such as big businesses and parts of government, may be.

**7.1** You need to know **where** invoices must go.

- Your invoice may need to be sent for authorisation to the buyer you deal with.

**7.2** Large organisations may decline to pay your invoice until they receive a **statement**.

- Send statements as early as you can in the month, every month.

**7.3** Your vital invoice may be **gathering dust** in someone's in-tray.

- Call the buyer to ensure it has been signed off and put into the payment system.
- Then phone the accounts office to confirm it has been received.

**7.4** You must not miss the **cheque run**.

- Many organisations will only print cheques once a month.
- Find out the date and call a few days before the cheque run to ask for confirmation that you will be paid.

## Expert contributors

Thanks to **Kate Beddington-Brown** (Institute of Credit Management, 01780 722900); **Frank Thaxton** (Thames Valley Partners, 020 7637 1727).

## Further help

There are other Start-up Briefing titles that can help you. These briefings are referred to in the text by name, such as **Pricing your product or service**.

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