

## Giving credit and getting paid

Having an effective credit policy in place before supplying goods or services is critical for the effective control of cash flow in your business. Before giving credit to any new customer, some time should be spent ensuring your business will be protected if the debtor has difficulty meeting payments. Time spent doing an initial credit assessment can save money and frustration.

### Should I give them credit?

Before making a decision about giving credit you should gather and evaluate some information about the applicant. The assessment of a new account doesn't require guesswork. There is a certain amount of readily available information that should be gathered before granting credit to any new customer.

The following checklist can be used to assess a customer's credit risk:

- ✦ Trading name – does this differ from the registered name?
- ✦ Where is the registered address?
- ✦ Names of the business owners, directors, etc.
- ✦ Business structure – is it a company, trust, sole trader, or partnership?
- ✦ History of business – when did the business begin operating etc?
- ✦ Business premises – are these owned or leased?
- ✦ Details of banker – which bank do they use?
- ✦ Trade references – what do other suppliers say about this customer?

If further information is required, the following additional sources can be considered:

- ✦ Trade suppliers;
- ✦ Mercantile Gazette, newspapers, and trade journals;

- ✦ Credit bureaus;
- ✦ Sales staff; and
- ✦ Published financial statements/annual reports.

### How can I protect myself?

Where possible it is always best to obtain some form of security from credit customers to protect your business. Four types of securities are set out below.

#### 1. Third party guarantees and personal guarantees

These are guarantees given by individuals (often company directors) to suppliers or creditors. Individuals give the suppliers or creditors access to their personal assets if the debt to the supplier is not paid.

#### 2. Caveats over property

A caveat is a prohibition that prevents a person from obtaining a further mortgage or selling a property without the consent of the person whom filed the caveat. Consent is usually given in exchange for payment of any debt secured by the caveat, or when the payment can be substituted with a fresh security.

#### 3. Mortgages

Mortgages over real estate (buildings and land) are powerful forms of security, because they give the mortgagee the right to sell the property where there is a default in payment.

## 4. Legal title in goods – Romalpa clause

The purpose of a Romalpa clause is to protect the seller from the insolvency of the buyer where goods have not been paid for. Title in the goods does not pass until payment is received.

Typically a clause on the invoice states 'Title will not pass until these goods have been paid in full'. Under the PPSA, the supplier will need to register the security.

### Early warning signals

To ascertain whether your customer is suffering financial difficulty, you need to find out about their business. This requires close monitoring that does not have to be time-consuming or expensive, and may help you avoid high debt collection costs or bad debts. Typical warning signals include:

- ✦ Comments such as 'We are suffering temporary cash flow problems';
- ✦ Adopting delaying tactics – unjustifiably complaining about work done or goods delivered or saying 'Can you send me a copy of the invoice?';
- ✦ The person responsible is always 'out of the office' or 'unavailable'; and
- ✦ Them not being aware of the debt or when it was due.

## Common customer excuses

Despite checking customers' creditworthiness, payment difficulties can still arise. The following is a list of common excuses and the responses you can use to encourage an earlier payment:

Customer	Response
The cheque's in the mail.	Could you tell me when it was posted, the number of the cheque, and the amount?
I'll have to check my records and get back to you.	I would appreciate that, but to save us time and money, could you please look it up now?
I'll call you back with the details.	I will make a note that you will call me back. If I do not hear from you this afternoon, if I phone you at 3pm, will you have the details?
The person who placed the order no longer works here.	Was the order personal or for use in your company?  PERSONAL: Can you tell me how I can contact them?

Before granting further credit to overdue accounts, a few basic questions must be asked. Some of the more critical ones are:

- ✦ Is the debtor short of working capital, ie cash?
- ✦ Is the debtor known to be in financial trouble?
- ✦ Does the debtor normally pay on time?
- ✦ Is the debtor's business growing or getting smaller?
- ✦ Has the debtor requested additional terms of payment before?
- ✦ Has the debtor suffered a significant reduction in staff numbers or has the business downsized?

### Next steps

Talk to us. If you want to set up a credit policy, we will be pleased to assist.

Remember, once you have set in place a credit policy, it will be up to you to use it effectively to get the best out of your business.

If you consider that any of the issues contained in this fact sheet may affect you, see us first.

### Disclaimer

Important: This is not advice. Clients should not act solely on the basis of the material contained in this fact sheet. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. We believe the contents to be true and accurate as at the date of writing but can give no assurances or warranty regarding the accuracy, currency or applicability of any of the contents. This fact sheet is made available to our clients as a helpful guide for their private information. Therefore it should be regarded as confidential and should not be made available to any person without our prior approval.

	COMPANY: Who uses the goods now? Can you put me through to them?
We have a cash-flow problem at the moment, and are awaiting a large payment. As soon as it arrives, I will pay you.	I am sorry to hear that, but I am sure you realise that your account is 30/60/90 days overdue. I suggest you arrange to send me a post-dated cheque, or pay the account in three instalments with three post-dated cheques.
We will not be paying this account until a credit note has been raised.	Could you tell me how much the credit is for? I suggest that you deduct this amount and send us a cheque for the balance with a copy of your invoice. When we receive your cheque we will adjust the balance of your account.

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