



DEBT COLLECTION GUIDE



About the 2022 NFIB **COLLECTIONS GUIDE**

This Guide was created to assist you in navigating current debt collections, as well as preventing them in the future.

Please remember that the NFIB Collections Guide does not constitute legal advice. Even with this Guide, you may wish to consult an attorney to determine applicable laws and regulations in your state.

ABOUT NFIB



The National Federation of Independent Business (“NFIB”) is the nation’s leading small business association, representing members in Washington, D.C., and all 50 states. Its membership spans the spectrum of business operations, ranging from sole proprietor enterprises to firms with hundreds of employees. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB’s mission is to promote and protect the right of its members to own, operate, and grow their businesses.

ABOUT THE NFIB SMALL BUSINESS LEGAL CENTER



The NFIB Small Business Legal Center (“Legal Center”) is a nonprofit, public interest law firm, established to provide legal resources and be the voice for small businesses in the nation’s courts through representation on issues of public interest affecting small businesses. In addition to our legal advocacy, the Legal Center frequently provides educational resources to aid small businesses in their daily operations. These resources run the spectrum from compliance guides such as this one to monthly webinars and tip sheets.

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SMALL BUSINESS
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COLLECTIONS

One of the most troubling aspects of running a small business is a customer failing to pay what they owe. Unfortunately, this is a problem that most business owners, especially those who offer a service that requires issuing invoices, will encounter.

Despite the frustrating and stressful nature of this issue, there are effective ways to avoid nonpayment and recover payment before resorting to legal action. Developed by the NFIB Small Business Legal Center, the NFIB Collections Guide was written to help you not only navigate your current debt collection issues but also help prevent them in the future.

This Guide is just one of the many compliance guides developed by our Legal Center to make your job just a little bit easier. To find out about all of the guides available in this series, call 1-800-NFIB-NOW or visit www.NFIB.com/LegalCenter.

Taking Preventative Measures

Sales Agreement:

The most important preventative step you can take to avoid nonpayment is to ensure both your business and the customer have a mutual understanding and agreement on the obligations of each party. Doing this verbally is NOT in your best interest. To properly protect you and your business, you must commit the terms of the agreement to writing. Terms in the agreement should include:

- The service you will perform, and/or goods rendered. The more specificity the better.
- Price you will be paid for the goods/service.
- How you will be paid (payment types).
- Dates that payments are due.
- Interest to be charged for overdue payments.
- Provision where customer agrees to allow you to place a lien on their assets if they do not pay.
- Whether disputes will go through mediation or arbitration.

Information on written service agreements can be found [here](#). Information and sample contracts for the sale of goods can be found [here](#) and [here](#).

Credit Checks:

When dealing with large dollar amounts, it is crucial to perform credit checks before entering into the contract. You do not want to enter your business into an agreement with a customer who has a history of not paying their debts. Throughout the process, it is important to be persistent, polite, professional, and prompt.

Invoice Tactics:

Even though it is the responsibility of your customer to pay for your goods or services, it is up to you to follow through with invoices according to the agreed-upon payment schedules. For long-term work or sales agreements, your customer will likely want to pay in smaller periodic installments rather than one lump sum. Set the expectations from the start in your contract or written service agreement. It may be helpful to add late fees and interest for late payments to incentivize prompt payment.

Missed Payments**When a Client Misses Payment:**

When a client has missed a payment, do not assume the worst or become accusatory. Doing so could damage the relationship between your business and this customer. Customers who feel slighted or offended by a business owner may resort to leaving negative reviews online or failing to make further payments out of spite.

In the case of a missed payment, it could be that your invoice was lost in a sea of emails or letters, and the missed payment was a simple oversight.

Begin by sending a friendly reminder to your customer or calling to remind them of the overdue payment. As time passes without payment, you should become more forceful in your requests. It is important to note that the reminder should be sent promptly if payment was not received by its due date. Depending on the customer, circumstances of the nonpayment, length of the business relationship, and amount of payment involved, you may consider giving your customer a grace period to maintain friendly relations.

If letters are failing to reach your client, attempt to call them or set up a face-to-face meeting. This can help begin to resolve the issue in a more efficient manner instead of waiting on their response through email. If the customer you are dealing with is running into financial trouble, contacting via phone or in person can be a good way to negotiate a revised payment plan. **ANY EXTENSION OR COMPROMISE SHOULD BE IN WRITING!**

If the customer avoids your communications, ignores you, or simply refuses to pay, you must then decide how to proceed. In this situation, you may wish to communicate a demand for payment.

The Demand:

When you have yet to receive payment and need to move to the next steps, start by writing a debt collection letter (see final page for template). This will be a formal demand for payment of the amount owed. This should include a reminder outlining the payment you are owed, the date it was due, forms of payment you accept, when you expect payment by, and any other pertinent information. In this letter you can state that any unpaid debt will result in further action (see more below). You should send this demand by certified mail to ensure the customer receives it and to be notified when the customer receives the demand.

Post-Demand Negotiation:

After your demand letter, you should continue to contact your customer to negotiate a proposed resolution. Often courts will look poorly on legal action if the creditor has not offered the debtor some type of solution. Here are some examples:

- Payment Compromise—Offer to forgive some of the debt if the client pays the rest by a certain date. ("If you pay 80% within two weeks, I'll forgive the other 20%").
- Payment Extension—Offer a longer-term payment schedule that will reduce the amount of the installment payments. If a \$1,200 payment was due within one month, offering to make it due in three months reduces the weekly payments from \$300 to \$100.

Final Letter:

If you have completed the above steps without receiving payment, you may wish to send one final letter prior to filing a lawsuit. This letter can mimic your debt collection letter, but also state your decision to file a lawsuit and that any

future communications may be through legal representation (depending on the amount owed and type of legal action initiated).

Process to Recover Debt After Demand and Negotiation

UCC Lien:

File a UCC Lien on the debtor's assets with the Secretary of State's office. You can only do this if the debtor agreed to grant a lien in the original agreement. Filing a lien will help prioritize your debt if the customer files for bankruptcy.

Arbitration/Mediation:

Arbitration is like a court case, but to a much smaller degree. Costs can become as much as actually going to court. Arbitration services are available at www.adr.org. In contrast, mediation is where both parties sit down with a neutral party and a compromise is reached.

Arbitration and mediation are only available if the original agreement signed by both parties agreed to arbitrate or mediate disputes.

Small Claims Court:

The quickest form of legal action you can take is filing a claim in small claims court. An advantage of small claims court is that you don't need an attorney to represent you. Some states even prohibit attorneys from participating in small claims court. States, however, each have their own limit for how much can be paid out in a small claims court. These limits can be found [here](#). Another advantage of filing a suit in small claims court is the simple fact that if your debtor fails to show up, you will win the case by default.

If you are dealing with an out-of-state customer, then a default judgment by your own state's court may not be enforced in another state. If your customer is out of state, then you may be better served by filing in small claims court where the customer is located. Expenses to do so, like travel and lodging, are tax-deductible.

Once you have a judgment from small claims court, you will need to apply to the court clerk's office for an execution on the judgment.

Collections:

If the amount owed exceeds the maximum small claims court limit in your state, your best course of action would be to take your claim to a collection agency. Collections agencies survive on collecting a percentage of your owed debt. The simple downside is the fact that you will not get 100% of the money owed; however, using a collection agency can often outweigh the time and money spent preparing for and participating in a civil lawsuit. If your customer disputes the amount of the debt owed, then the collection agency cannot pursue the debt and will tell you to hire an attorney. You can find more information about how collection agencies operate [here](#).

Debt Factoring:

If you are in a tight cash position, you can utilize a factoring service. These intermediary agents will purchase your accounts receivable for a determined percentage of the account's value. The factoring service will then own the debt and have to collect your customer's money. After doing so, they will send you the remaining amount owed on the account minus a percentage withheld for their service. The biggest advantage of using a factoring service is receiving cash up front, rather than waiting for a collection agency to collect it. You can find more information about factoring [here](#).

Example:

- You sell your \$20,000 dollar account from Customer Y to Debt Factoring Company A for 80% of the total debt. Up front your business would receive roughly \$16,000.
- Debt Factoring Company A collects the entire \$20,000 debt from Customer Y.
- Debt Factoring Company A then pays you the remaining \$4,000 from the total debt, minus its factoring fees.

WHAT NOT TO DO!

- Do NOT post negative reviews online!
 - Doing so can open you up to a civil lawsuit for defamation if anything you say is not 100% factual.
 - Can also backfire – new customers may view this as unprofessional.
- Do NOT misrepresent yourself or the facts!
- Do NOT threaten the customer with jail or criminal penalties!
- Do NOT call at unusual hours. Keep your calls limited to between 8 a.m. and 8 p.m.

More Information

For more information on recovering an unpaid debt, please review this NFIB Small Business Legal Center webinar on Collections with attorney Cliff Ennico.

Please refer to the debt collection template on the next page

[YOUR LETTERHEAD]

[date]

_____ [name and address of deadbeat]

VIA CERTIFIED MAIL,
RETURN RECEIPT REQUESTED

RE: NONPAYMENT OF AMOUNTS DUE TO
[YOUR COMPANY]

Dear Mr./Ms. _____:

Please be advised that I am acting on behalf of _____ [your company name] (the "Company"), to whom you owe \$_____, together with accrued interest of \$_____, for services rendered pursuant to the attached invoice dated _____, 20__.

The Company has contacted you a number of times to obtain payment of your overdue account. Despite these efforts, and your repeated assurances that all overdue amounts will be paid in full, you have not paid the Company's overdue account.

Please be advised that the Company intends and has authorized its attorneys to take all available legal action against you personally in this matter. This will be done forthwith if the Company has not received the foregoing amount in full by the close of business on _____, 20__ [10 to 14 days from the date of the letter is customary].

Kindly remit payment in full to the undersigned, by bank or certified check, payable to "[Name of Your Company]" by this date to avoid further action. Your agreement with the Company provides for accrual of interest at ___% per annum (___% per month) which will continue to accrue until the Company has received payment in full of its outstanding invoice. Interest shall continue to accrue from the date of this letter at ___% per annum or the highest rate allowed by law if less. As a final matter, I call to your attention that if payment is not received in full by _____, 20__ as aforesaid the Company will seek payment of its legal fees and expenses, in addition to the amounts owed and accrued interest, in any action brought against you.

Please direct all future correspondence in this matter to my attention.

Very truly yours,

cc.: [name and address of your company's attorneys]



IF YOU HAVE A QUESTION,

a story of government abuse of a small business,
or a precedent-setting case, please give us a call.

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