



MasterCard Working™
FOR SMALL BUSINESS

Susan-Says®:

Protect yourself from a customer's bankruptcy.

By Susan Wilson Solovic, CEO SBTV.com

Many years ago, I owned and operated a small boutique advertising agency. I enjoyed the close relationships I had with my clients, becoming almost part of the family in a couple of situations. One client in particular was a family-owned business in the process of expanding through franchising. They referred to me as their adopted daughter.

My company handled marketing for the franchisor and franchisees. And because of the rapid growth of the business, this company soon accounted for about 80 percent of my business. That was my first big mistake. My second mistake -- not cutting them off when they first began having financial difficulties. They went bankrupt. As a result, I was left with thousands of dollars of unpaid bills for my services and owing a number of additional vendors who I had hired to work on the account as well.

In hindsight, I should have known better than continue to provide services to a customer who was falling behind on paying their suppliers. But because they were such a large client, I was afraid to confront them for fear I'd lose the account. However, even the most careful manager can find his or her business in jeopardy because of a customer who files for bankruptcy protection.

Imagine what would happen to your business if one of your largest customers filed Chapter 11 owing you thousands of dollars. Many businesses are unable to recover from such a disaster and eventually are forced to liquidate.

“When one of your customers files bankruptcy, you have little or no protection under the bankruptcy laws. A lot of business owners are surprised to learn that,” explains Chris Kelleher who owns The Law Firm for Business and who specializes in working with growing businesses. “I have to remind my clients that regrettably the bankruptcy courts were built for the debtor, not for the creditors.”

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In order to protect yourself from a customer's business failure, don't be too quick to push product out the door. Frequently, when trying to increase sales and capture market share, businesses extend too much credit to people who don't deserve it.

If you are dealing with a first time customer, CPA Gavin Poppen, a principal at Poppen & Associates, says do your homework. "Check to see if the company submits financials to Dun and Bradstreet. If they do, you can do financial research on the company."

"It's difficult for a business that is trying to grow and expand in a competitive industry to have a tough credit policy, particularly in hard times," Kelleher says. "But, when you extend credit you really need to screen your customers carefully.

Here are some red flags to watch for:

- **Tax problems, liens and lawsuits.** Companies often file bankruptcy to forestall attempts by its creditors or the Internal Revenue Service to seize its assets. Pending tax liens, other liens or lawsuits could signal the customer is in trouble.
- **Changes in payment patterns.** Signals to watch for include partial or sporadic payments by a customer who formerly paid in full; delay in payment of 60 days or more by a customer who used to pay promptly; a dramatic increase in a customer's volume of orders, with the same monthly payment; and frivolous complaints to reduce the bill or to delay payment.
- **Management turnover.** While management changes may be necessary turnover among top and middle management can signal trouble, particularly if the customer constantly replaces its chief financial officer or other top financial personnel.
- **Breakdown in communication.** Unreturned phone calls, unanswered correspondence or managers who are always unavailable are circumstances which should trigger a review of that customer's credit status.
- **Bad news.** A firm should keep its ear to the ground for unfavorable information about its customers. Local and business newspapers, trade associations, credit services and Securities and Exchange Commission reports can be good sources. Although such information sometimes is unreliable, it nonetheless can serve as a starting point for making further inquiries about a customer.
- **Increasing reliance on the company.** While it may be flattering for a firm to obtain an ever-increasing share of a customer's business it should be wary if this occurs. Sometimes the reason for the increase is that the customer is being cut off by its other suppliers and has no one else to order from.

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- **Layoffs and downsizing.** While layoffs and downsizing may be inevitable in a recession, a company should be wary of a customer who has to cut not only the fat but also the muscle and bone in order to survive.

The bottom line is that while you may be managing your own business well, your customers may not be doing the same. Surviving a customer's bankruptcy is a matter of good planning, vigilance and professional advice.

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