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Be careful when giving customers credit

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In today's tough economic times, it's not uncommon for a business to extend credit to its customers to facilitate a purchase.

Under this scenario the business provides its goods or services on faith that the customer will make payment within an agreed-upon time frame.

Unfortunately, not everyone keeps a promise, making it that much more critical for businesses to carefully weigh the risk of extending credit and to put proper safeguards in place to limit their exposure and ensure prompt payment.

"You have to be cautious about extending credit," says Michelle Dunn, author of "The Ultimate Credit and Collections Handbook" (Entrepreneur Press; \$19.95) and president of The American Credit & Collections Association in Plymouth, N.H. "The best way to limit your risk is to not go into it blindly."

Since getting paid is particularly challenging in the current economic climate, it's important to consider these precautions before extending credit:

Establish a credit policy: It can be short and sweet but should outline the guidelines under which you extend credit, including collection methods and follow-up, says Dunn.

Do risk assessment: Before extending credit, determine how much risk your company can take if the debt is unpaid, taking into account product costs and other factors, says Marco Carbajo, author of "Eight Steps to Ultimate Business Credit" (available via free download at businesscreditblogger.com) and president of Business Credit Insiders Circle in Novi, Mich. This will help you set limits, he notes.

Assess creditworthiness: Have the people complete a credit application, says Dunn. "It gives you permission to check their credit or call references," she explains. Preferably, they



should list three references, including their bank, and it should be updated every six months, she notes.

Check credit: See whether the business is registered with Dun & Bradstreet and run a credit check, says Carbajo. You could establish benchmarks in your credit policy that say, for example, that to receive credit the business must be listed with D&B, which offers credit limit recommendations, he says. You can also run checks via [Experian](#) or [Equifax](#).

Do a site visit: Visit the business' location and ask good questions regarding financials, ability to pay, etc., says Neil Seiden, managing director of Asset Enhancement Solutions, a financing/turnaround consulting firm in Port Washington. "People tend to be more honest with you if you meet them in person," he says.

Get a guarantee: If they'll agree to it, you can ask customers for a standby letter of credit that would be issued by their bank guaranteeing all or part of the money, says Seiden.

Minimize your risk: There are ways you can limit your exposure, including extending less credit or requiring a down payment, notes Seiden.

Get credit insurance: This insures accounts receivables against losses due to insolvency and delinquencies, explains Joel Berman, president of Credit Insurance International Risk Management Inc., a credit insurance broker in Smithtown.

Graphic Paper, a wholesale paper distribution company in Central Islip, has found it to be quite helpful. It protects extensions of credit over \$25,000, says Chief Financial Officer Anthony Aronica, who pays about \$100,000 annually in premiums. "In the past couple of years, we've had to use it more often than, say, five years ago," said Berman, who also has clients complete credit applications and conducts credit and reference checks.

Join industry groups: Joining an industry credit group like the National Association of Credit Management can provide insight into customers' payment history, says Aronica, who is a member. It tracks and shares among members critical credit information about mutual customers. "They have a good database of the buyers we do business with," he says.

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