Offering Credit to Your Customers

In recent columns I have discussed doing business with checks, cash only, and credit cards. After reading these, one local business owner advised me last week to pass on that the best policy is “No Checks” period. Obviously he had experienced, first hand, the terrible problem of trying to collect on a bad check. On a related note, how should a business owner consider the often used practice of extending “credit” to your customers?

By extending credit to your customers, you give them the option to purchase products or services today and pay for them at a later date. When your business accepts credit card payments and personal checks or invoices customers, it is essentially extending credit on the assumption that customers have the funds to pay for the transaction.

When you extend credit to customers through card payments, the credit card company manages the risk. When you extend credit through invoices or personal checks, you are responsible for verifying and accepting payments and managing the risks that come with them.

Extending credit through invoices is common in some industries such as construction or manufacturing, but may not be practical for every business. To decide if extending credit is right for your business, weigh the associated rewards and risks. Here are a few check points to consider:

- The option of credit enables customers to focus less on prices, enhances customer relations, and has the potential to generate more sales.
- Extending credit costs money. When you sell something on credit, you will not have payment on hand and will need to temporarily recoup the cost from other areas of your operating capital.
- If customers don’t pay, you could be in for a long settlement process that may not end in your favor.
- Ask yourself if you have a significant business need to extend credit. Extending credit could be the factor that keeps your business afloat if it makes it easier for your customers to buy from you. Nevertheless, if it isn’t necessary it may not be worth the extra time and paperwork.

So, if you decided to offer credit, I suggest that you establish credit practices before you begin. Be sure to establish detailed policies and understand consumer protection laws. Include these considerations:

1. Determine to whom you will extend credit such as individual customers or other businesses. Run credit checks on all customers before you agree to extend credit.

2. Develop clear, consistent payment guidelines. Your bills should indicate when payment is due, when it will be considered delinquent, and who to contact with questions.

3. Determine how you will bill or invoice customers. Will you or your employees mail requests for payment yourselves, or will you hire another company to handle invoicing?
4. Create a plan for collecting late or defaulted payments. Regardless of the type of application or documents you use for credit transactions, be sure to get all of your customers' information in writing. In return, provide them with a copy of your payment policy, which spells out how penalties will be applied to late payments and how you will handle unpaid bills. It's important to have this documentation in case a fraudulent or delinquent credit transaction occurs.

5. If your business extends credit to customers, you should become aware of consumer credit laws. The Federal Trade Commission (FTC) enforces the nation’s consumer protection laws. These laws regulate how you advertise interest rates, how much time you have to respond to billing-mistake claims, how aggressive you can be when attempting to collect a debt, and other aspects of extending credit and debt collections.

Planning and managing your business finance strategies can be complex. If you need help with this aspect of your business, contact America’s free and confidential source of small business mentoring and coaching, **SCORE**.

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