

What to do When You Haven't Been Paid: Recovery Options for Secured & Unsecured Creditors

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You supplied materials or services per the contract or purchase order, now your customer needs to pay for those materials and services. Just because they *need* to pay you doesn't mean they *will* pay you - it's a tale as old as Mr. Jefferson himself (*if he were still alive of course*).

Whether you are a secured creditor or an unsecured creditor, slow-paying and non-paying customers are, at the very least, frustrating, time consuming and often costly burdens.

This article will provide you, the secured or unsecured creditor, with some recovery options in the event you are unpaid. These recovery options may not be "new and groundbreaking." These options may even seem too simple to be effective. But don't underestimate their power and success!

The True Cost of Write-Offs

Before delving into tips on collections and the remedies for secured & unsecured creditors, you must understand the true cost of a write-off and weigh that cost against the cost to proceed with collection efforts.

The cost of write-offs to a company can be crippling. A write-off of \$50,000 at a 30% margin means you would have to generate \$166,666 in additional sales to recover that lost profit. If you operate at a 15% margin the additional sales mushroom to \$333,333.

It may not be an issue when one customer is slow paying, but it's never just one customer; it is several customers and it can have a significant impact on cash flow. If you have 10 accounts paying an average of 20 days late and each is invoicing at \$50,000 you could have \$500,000 + outstanding.

How to Make the Collection of Unpaid Monies Easier

You have likely heard this dozens of times, if not more, but it's critical to start the collection of unpaid monies the moment they become past due. Here are a few steps on how to make the general collection process easier.

- **Monitor open invoices:** Routinely review open invoices and as soon as an invoice is past due (e.g. If you bill on 30 day terms, day 31) contact your customer and inquire on the invoice.
- **Try multiple mediums:** Use phone calls, emails, demand letters, etc. & make sure you keep track of your communications – good record keeping is important!
- **Pay attention to cues:** Social cues & non-verbal cues are frequently early warning signs that an invoice (or customer) is going to be an issue. When people stop communicating they are sending a clear signal "I can't/won't pay the invoice, and maybe if I ignore you, you will go away."
- **Check status:** Note changes with your customer's business, such as a disconnected phone number, undeliverable mail or email, and changes in their corporate status with the Secretary of State.
- **Review credit:** Credit reports can provide a wealth of information, especially for payment history, DBT changes, recent collection placements or judgments.
- **Cut them off:** If you have invoices that a customer isn't paying, stop extending them additional credit. Debt is like a beast and if you continue to feed it, it will gobble up every last bit and give you nothing in return.
- **Know when to let it go:** Don't immediately toss the invoice into the bad-debt-write-off-pile. "Let it go" from your desk and move it to the desk of a specialized collection agency. Collection agencies are

trained and experienced, not to mention, a third party is sometimes more effective simply because they are a third party – removed from the situation.

Get Paid as a Secured or Unsecured Creditor

Mechanic's Liens and UCC filings are two of the greatest fiscal weapons available to the construction credit professional. Mechanic's Liens and UCC filings, when properly executed and perfected, provide you with leverage. These remedies put you in the position of a secured creditor and without question, being a secured creditor is the only place to be.

The Power of the Demand

Whether you are a secured creditor or unsecured creditor, a well-crafted demand letter can expedite payment, allow you to maintain control of your collection process and save you money.

The demand letter is a strongly worded request for payment, most often served upon your customer, advising legal action may be taken if payment is not received within a specified time period. In order for a demand letter to be successful, it should contain factual information and be succinct.

The demand letter should include the date of the demand, your company's name & contact information, your debtor's name & contact information, a reference to the debt (i.e. provide the project name, the UCC filing number or purchase order number), the amount of the outstanding debt, the due date of the debt, how the debt should be paid and the consequence for not paying the debt.

The party(s) involved need to know there is a consequence for not paying you – this is where you can leverage the security of the UCC filing or mechanic's lien. Be specific and provide a realistic ramification for not paying - a few examples:

- If secured by a mechanic's lien *"...If payment is not received, we may pursue all available legal remedies against you, including, but not limited to, filing a mechanic's lien"*
- If secured by a UCC filing *"...if payment is not received, we may pursue all available legal remedies available under the Ohio Uniform Commercial Code."*
- If unsecured *"... if payment is not received, we may pursue all available legal remedies against you, including, but not limited to suit."*

The demand should be served upon your debtor, but it is recommended you also send a copy of the demand to any party that may contribute to you being paid.

- *"I supplied to a construction project"* - If the debt is related to a construction project, the additional parties you may want to include are the project owner, project manager, prime contractor, subcontractor, lender and surety.
- *"I supplied inventory to my customer"* - If you applied for or have filed a UCC as security, serve a copy of the demand solely upon your debtor.

Secured through the Mechanic's Lien/Bond Claim Process

A successful mechanic's lien/bond claim program begins with a successful preliminary notice. Solid project information and complete contractual chain information are the foundation of the preliminary notice - this information should be obtained on every project as standard business practice.

Once a mechanic's lien process is in place, and preliminary notices are being served regularly, 96% of the time, properly serving a preliminary notice will get you paid, with no additional action needed. A 96% success rate is huge and the primary driver behind that success is that everyone within the contractual chain knows you are supplying to the project and taking steps to secure your rights as a creditor - there is transparency.

Typically, preliminary notices will result in timely payment 96% of the time, but that does leave 4% unpaid. It is likely that 4% of a company's projects will require the filing of a mechanic's lien, and less than 1% of projects will require a company to proceed with suit/foreclosure. If you find yourself unpaid and in the frustrating 4%:

- **Send a Demand Letter** before proceeding with a mechanic's lien. Often times, slow-paying clients will respond to the force and time constraint of a demand letter, without you having to spend additional funds on a mechanic's lien.
- **File a Mechanics Lien:** If the preliminary notice and subsequent demand letter do not prompt payment, then it is time to proceed with a mechanic's lien. It is recommended to have copies of invoices, bills of lading, the statement of account and copies of various communications, to support your claim. (Some states actually require the invoices be attached to the mechanic's lien when sent for recording.)
- **Proceed with Suit:** In the event you remain unpaid, the final step is to proceed with suit (also referred to as foreclosure) in a court of law to enforce the mechanics lien. Suit is typically a slow (and costly) process, due to the various facets of litigation. It is best to utilize an attorney who is well versed in construction/mechanics lien laws and familiar with the project itself (including issues surrounding change orders, back charges, etc.).

Don't be afraid! Too often, companies are led to believe that by protecting their rights to get paid, they will jeopardize projects and relationships. Companies fear that sending preliminary/prelien notices and securing mechanic's liens, will somehow align stars so that the world implodes. OK, an exaggeration, but the fear is real and it shouldn't be. Mechanic's Lien and Bond Claim laws are there to protect parties supplying to construction projects. If you take the steps to secure rights and get paid without having to enforce those steps, then no harm no foul, but if you don't take steps and don't get paid, well...

Additional Tips

- **Give yourself a fair chance:** Negotiate a fair contract. No-lien clauses, pay-if-paid and pay-when-paid clauses all can limit your ability to collect your money.
- **Make sure you are providing the exact documentation required for payment.** Public projects in particular can have very specific requirements for payment. Waivers of lien, certified payroll reports, and current certificates of insurance all can be required in your invoice package. Make sure you know what documentation is required and provide it. Also know when your payment request must be submitted, and what all can be included. Can you include stored materials? Are you forecasting for a few days? Make sure the weather is going to hold up!
- **Contact other parties on the ladder of supply:** Make sure the story you are hearing is the true story. Every project has different subcontractors, general contractors, and owners. They all can affect your payment. If your customer is a subcontractor and they tell you they have not been paid by the general contractor, verify this with the general contractor.
- **Know the prompt pay statutes for the particular state, and use them to your advantage:** Nearly all states have prompt pay statutes for public as well as private projects. They outline how quickly parties on the ladder of supply must remit payments to their customers once they have received payments. They also limit the amount of retainage that can be withheld. Does the statute limit retainage to 5% but your customer is holding 10%? Make sure the playing field is level.
- **Use exact lien deadlines in collection calls:** Using the exact deadline sends a message to the debtor that you have that particular project on your radar and are serious about filing a lien if you are not paid.

All parties supplying materials or labor to a construction project should take the appropriate steps to secure their mechanic's lien and bond claim rights – all parties, all projects, all the time, no exceptions.

Secured through a UCC Filing

Just like the mechanic's lien process, serving a demand letter is a great starting point for recovering funds. In the event the demand letter does not prompt payment, you may need to proceed with further legal action and the next action is dictated by the type of UCC you filed.

Did you file a PMSI UCC: If your customer has defaulted on payment(s) and you have filed a Purchase-Money-Security-Interest (PMSI) UCC, you need to determine whether or not you would like your equipment/inventory (aka goods) back.

- If you do not want your goods back, you can place your claim with an attorney to file suit. By filing suit, you may receive Judgment, which allows you to garnish accounts and/or attach to assets.

- If you do want your goods back, and your customer has the goods, you have the right to repossess without disturbing the peace.

If you are unable to peacefully repossess the inventory/equipment, you could take legal action by filing a temporary restraining order or by filing suit against your debtor.

Did you file a Blanket UCC: If your customer has defaulted on payment(s) and you have filed a Blanket UCC, you could place the outstanding debt with a collection agency or file suit against your debtor.

Secured or Unsecured - Seek Assistance from Collections Agency

Managing the overall collections process starts with securing your receivables, so this “last step” may seem a little out of place. As mentioned at the beginning of this article, partnering with a collections agency can save you time & money, not to mention the likely increase in recovery of unpaid funds.

If you have security, like a mechanic’s lien in place, choose an agency that knows how to leverage that security in the collection process.

Make sure to provide the collections agency with any and all documentation regarding the past due account. This may include: copies of the Mechanic’s Lien or UCC filing (plus a copy of the Security Agreement), the Contract or Agreement, the Credit Application, invoices and Statement of Account, the Proof of Delivery, the Personal Guarantee, Correspondence & Notes (emails, letters/demand letters, phone conversations), Corporate Certificate (this should include your debtor’s legal identity, including whether it is a corporation, partnership or proprietorship) Credit Report(s), and your customer’s Trade References, including bank name and account number (include copies of the Returned/NSF Check(s)).

Don’t Wait

Whatever steps you take, make sure you don’t let that receivable age for too long. It is a well-known fact, and long studied trend, that the longer an account remains past due the harder it becomes to collect.

Per the results from a survey hosted by the Commercial Law League of America “...*the probability of full collection on a delinquent account drops dramatically with the length of delinquency... even after only three months, the probability of collecting a delinquent account drops to 68.6%. After six months, collectability drops to 52.1%. And after one year, the probability of ever collecting a delinquent account drops to 9.3%.*”

About NCS

Since 1970, NCS has been the leader in providing credit professionals throughout the U.S. and Canada with proactive solutions to secure receivables, minimize credit risk and improve profitability.

With our distinct service groups: Construction, UCC, and Collection – NCS develops customized solutions based on your business model and organizational requirements to Secure Your Tomorrow®. NCS has educated more than 400,000 credit professionals on securing their receivables and reducing their risk through NCS events, resources, and social media. NCS offers software and web based solutions such as LienFinder™, The National Lien Digest®, LienTracker®, and Lien Direct Online. These resources help manage credit risk, provide time and information requirements, monitor deadlines and generate notices.

Protect your receivables by partnering with NCS. Contact us to see how we can assist you in developing a UCC, Mechanic’s Lien or Collection program.