

# Falling Behind DELIQUENT ACCOUNTS

by Kathleen Harrell-Latham and Mark Geier

In the current economy, an increasing number of otherwise good customers are falling behind on their bills. As a creditor, take a proactive approach to increase your return and your own profitability. This article summarizes some important steps to protect your interests.

## Collection Starts with the Contract

Contracts do not have to be lengthy to include terms that may aid in collection. Many companies include terms in their signed agreements or in the “terms and conditions” section of their quotations, purchase orders, acknowledgments and invoices. These provisions include the date payment is due, the ability to recover attorneys’ fees in the event of default, rate of interest or late fees for delinquent payments, and the state law, jurisdiction and venue for any disputes. These are just a few common provisions, but they can be surprisingly helpful to avoid disputes and streamline the collection process.

Also, if an account starts to show signs of trouble, take action to strengthen your position. Depending on the law, you might stop further work or deliveries, convert the account to COD, or require personal guarantees for continued sales.

## Know Your Debtors

Many creditors do not know who is legally responsible for their debt. This has become more of a problem as larger businesses create more subsidiaries, divisions or affiliates. Your contracts and sales documents should identify all of the parties who will be liable, using their legal and assumed business names whenever possible. The secretary of state will provide the information online, but you may need an attorney or paralegal to interpret the codes.

Creditors often do not research a customer’s name until the account is delinquent. Even then it is better to list all of the responsible parties. But beware: A creditor must have a legal basis for

making a claim against any business or person not listed in the sales documents themselves.

## Liens or Collection Agencies as an Alternative to a Lawsuit

Statutory liens can be an effective alternative to a lawsuit. These liens are highly specific in nature and often require continued possession of the goods. Another important consideration is whether there are any additional steps necessary to perfect the lien and its priority. The specifics of what and where something needs to be filed depends on the goods at issue, and the state law in which the buyer and goods are located.

Some companies hire collection agencies to assist them. Shop around for the best return and read the fine print. How do you move an account from the collection agency to your law firm?

## Prompt Action Upon Default

Act promptly when an account first becomes delinquent. Immediate and repeated contact gives you a better understanding of the customer’s financial circumstances. This information helps you evaluate whether and how quickly to pursue collection. Also, each state has its own timeframes for starting a lawsuit. If you miss these deadlines (also called statutes of limitation), you cannot collect the account. While most of these deadlines are fairly lengthy, some are not and some are quite technical. Your attorney can advise you.

## Lawsuit Options

If you decide to sue, consider your options. Some contracts have a mandatory arbitration provision that may control.

Otherwise, if the amount is relatively small, start the lawsuit in conciliation (small claims) court. Each state varies; conciliation courts in Minnesota may hear claims of up to \$7,500. Typically, these claims can be pursued without an attorney. Information about the forms, the fees, and the process can often be

found on the court’s Web site. However, be aware that the debtor can dispute the debt, countersue and at times move the lawsuit to District Court. So there are material risks.

Another option is to proceed in State District Court, especially if the debt exceeds the limits of conciliation court. Before doing so, check whether your company must be represented by an attorney.

Minnesota offers you the unique ability to start a lawsuit without immediately filing it in State Court. This “pocket service” can be an effective tool in settlement negotiations because the information about the debt does not become “public” until you file the lawsuit. In some situations, Minnesota also allows creditors to obtain payment before the judgment is entered. Consult an attorney to evaluate whether and how you can collect a debt without a judgment.

Finally, consider starting a lawsuit in federal court if the amount in controversy exceeds \$75,000 and the debtor is located in a different state. Proceeding in federal court may provide some strategic advantages depending upon the particular product at issue. However, litigation in federal court tends to be a more involved process and can be more expensive.

The first step to collecting delinquent accounts is to include helpful terms in your contract and sales documents. Then choose your path wisely, using an attorney as you deem appropriate. PM

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