

PROTECTING YOUR INVESTMENT: PART 1

Are You a Building Material Supplier or Are You a Bank?

If You Extend Credit to Customers You're Both

Every time you provide equipment or materials to a customer on credit, you are lending that customer money. Ask yourself: *"If I was a bank, would I provide this customer with a loan?"*

We all know that the construction industry is cyclical and the financial position of your customers is constantly changing. Regardless of whether or not you have an existing relationship with your customer, every credit-based transaction should require a quick analysis to determine that customer's credit worthiness at the time.

Questions to ask before extending credit:

- **Credit check** – How is the customer's credit? Many services will conduct a fast and relatively inexpensive credit search.
- **Recent history** – Has the customer been late on past payments?
- **Reputation** – Has this customer defaulted on contracts with others?

Even Creditworthy Customers Can Harm Your Business

Credit applications are legally binding documents that will preserve your legal right to collect money should your customer default. Key provisions of the credit application should include:

- ① **Specific provisions related to how disputes regarding payment will be handled.**

In some cases it is more cost and time efficient to require that disputes be resolved through arbitration rather than litigation.

- ② **A representation that the person(s) signing the agreement has full authority to execute the agreement on behalf of the applicant.**

Many defaulting customers claim that the person who signed the agreement did not have the authority to act on its behalf and, therefore, the agreement is void. To prevent this defense from being raised, credit applications should always include an agency clause.

- ③ **Personal liability should the borrowing business fail to pay its debt.**

One of the most important terms to include in a credit application is a personal guaranty. Through a personal guaranty, the customer is acknowledging that he or she is personally liable if the borrowing business fails to pay its debts. This allows the lending business to levy against a borrower's personal assets in the event of non-payment. Personal guaranties are critical in situations where you are attempting to enforce a judgment, especially where an officer of the borrowing business has more assets than the business itself.

The next edition of *Protecting Your Investment* will provide guidance on what suppliers can do when their customer goes out of business.

Before making your choice of attorney, you should give this matter careful thought. The selection of an attorney is an important decision. You may, if this letter is inaccurate or misleading, report same to the Committee on Attorney Advertising, Hughes Justice Complex, P.O. Box 037, Trenton, NJ 08625



LINDABURY

McCORMICK, ESTABROOK & COOPER, P.C.
Attorneys at Law

908.233.6800 • www.lindabury.com