THE WALL STREET JOURNAL.

It Just Isn't Working? Some File for Customer Divorce

As Weak Economy Exerts Financial Pressure, Firms Shed Their 'High-Maintenance' or Delinquent Clients

By RAYMUND FLANDEZ
November 10, 2009

It's the beginning of the tough-love era. Some small-business owners are ending relationships with aggressive customers who ask for more discounts and concessions or want more leeway on payment time.

Hampered by a slack economy, these businesses, mainly service providers, are cutting loose nonpaying or late-paying clients who divert resources away from more loyal or profitable clients. Last fall, many businesses retained customers by discounting, providing special payment terms or creating loyalty programs. But today, they can no longer afford to do so.

For the first time since she started her business five years ago, Kishau Rogers, owner of Websmith Group LLC in Richmond, Va., had to "drop or avoid clients that are high-maintenance or late payers." Some of her clients, mainly retail-store owners or entrepreneurs, often asked for discounts because of their own tight budgets or an expanded level of service beyond the agreed-upon contract.

As a result, by eliminating 5% of her clientele this year, the 36-year-old is saving 20% more of her time while the Web-site development firm's 2009 revenue is on track to rise 10%. "It was the best decision I've made, because it really reduced the level of frustration that I was experiencing," Ms. Rogers says. "It freed me up to the clients that are loyal and pay on time."

Still, the drastic action is bringing separation anxiety for some small-business owners. For years, many have prided themselves on customer service. And some small businesses, suffering from a drop in sales, fear they can't afford to be picky.

But problematic customers need to be fired, says Valarie Zeithaml, a marketing professor at the Kenan-Flagler Business School at the University of North Carolina at Chapel Hill. "That is a scary thing to do in an economy like this," she says. "But to have to continue to have a customer that's losing the company money with every transaction is not a good strategy either."

It is taking four days longer to collect receivables this year at an average of 27.4 days, compared with 23.7 days last year, according to Sageworks Inc., a private-company financial-data provider in Raleigh, N.C.

Alice Bredin, small-business adviser for American Express Open, says small-business owners should drop difficult clients carefully. As always, she says, "when you choose to no longer do business with someone, be courteous and professional."

This year, Ren Moulton, chief executive of Dogmatic Products Inc., a New York maker of pet toys and treats, has dismissed 30 out of 300 clients, mainly because of slow payments by the independent pet specialty stores.

Over the past year, Mr. Moulton has taken delinquent clients to task by calling them for payments. Some made up excuses or told him they forgot to pay, he says. "We understand it's a tough time for everyone," he says. "So sometimes, we'd let it go. After a while, it wasn't an efficient way to kind of run things." He adds that it isn't worth it for his 10 employees to spend five hours for an account that may only generate $2,000 in sales over the year. Dogmatic expects to post $4 million in revenue this year.

Now, he's doing more to protect his company, such as running credit checks for the first time on smaller accounts, sending contracts ahead of time and reiterating terms and obligations. For international clients, he now has a pay-upfront policy. Before, they only had to pay half upfront. "I do believe in firing bad accounts," he says.

Recently, Chris Cole, owner of a Riverside, Calif., franchise of Volvo Construction Equipment Rents Inc., received an urgent call from a dispatcher of a construction company who needed to rent some equipment the next day. He refused to fill the order immediately. The client had been 100 days behind in payments. It was a good decision. The next day, Mr. Cole received five local orders, which he wouldn't have had time to fulfill if he had rented out his equipment to the delinquent customer. Still, some maintain a relationship with troubled clients.

Ed Engoron, co-founder and president of Choclatique Inc., a high-end chocolate and confection maker in Los Angeles, decided to help out a client that entered bankruptcy court. He read about his client's predicament online in May and was worried that he would never receive the several thousands of dollars that Choclatique was owed. So, he talked to the Phoenix-based upscale grocer and worked out a deal where the debt is being set aside until the customer's finances improve.

"I want my company to be remembered as a company that worked with them and did not cut them off," he says. He adds that the client had always paid on time. The grocer is now placing holiday orders and making regular payments. "It's a sacrifice," Mr. Engoron says, "but it's a worse sacrifice if I don't have additional income coming in."