



Euler Hermes

# Collection Profile USA

## Collecting in the USA

- The payment culture of domestic companies is becoming increasingly uncertain and, in the absence of a harmonized framework on late payments, payment terms remain a mere contractual issue.
- The court system is complicated by a county, state and federal structure in which protection mechanisms are not recognized and where no simplified proceedings are available to settle the simplest files. As a result, significant delays and costs must be expected while enforcement may be difficult.
- When the debtor becomes insolvent, collecting debt becomes a complex task. The bankruptcy system remains pro-debtor and making a company insolvent is not a significant way to obtain payment. In practice, bankruptcy reorganization is resource-draining and rarely results in general unsecured creditors receiving any dividend.

## Collection complexity



## Complexity relating to

Notable → Severe

	Notable	Severe
Payments	\$ \$ \$	\$
Court proceedings	⚖ ⚖	⚖ ⚖
Insolvency proceedings	↘ ↘	↘ ↘



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Our knowledge serving your success

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## General information

### Availability of financial information

Obtaining financial information on private companies is rather a difficult and costly exercise in the US. It is possible to purchase financial information from specialized providers, but it is also recommended to obtain a detailed credit application, and if possible a personal guarantee when granting credit in the United States. Information, therefore, is the lifeblood of the Euler Hermes credit insurance business and our risk department has various tools available to allocate each company a grade reflecting its financial health and how it conducts business. Grades represent a core of our knowledge and analyses, and help clients identify and avoid risk. Data is continuously monitored to offer the most up-to-date information to support management decisions.

### Main corporate structures

Liability for business debts is determined by legal structures, which are described as follows:

- Sole Proprietorship is available for small businesses managed by an individual and for which no commercial structure is necessary. In this case, the owner is held liable for all business debts. Two or more individuals may also decide to share ownership and responsibilities through Partnerships, in which case the partners may be jointly and individually liable for the actions of the other partners. Limited Liability Partnerships alternatively offer limited liability to the partners.
- Limited Liability Companies (LLCs), S Corporations and C Corporations represent the great majority of businesses because these structures limit the shareholders' liability to the value of their contribution. In corporations, the business is controlled by a Board of Directors elected by the shareholders. In any case, a corporate shield protects the owners from any personal liability unless one can prove fraud, and various capital requirements may apply depending on the state selected for registration.
- Foreign companies may alternatively settle in the US through Branch Offices which provide no liability limitations to the foreign parent company, or through the creation of a subsidiary company in one of the forms listed above. Joint Ventures may also take the form of a partnership contract.

### Regulatory environment

The United States has a federal structure consisting of fifty states and one federal district (Washington, D.C.), each characterized by specific rules and specific courts.

Disputes are normally settled at the state level through State and County Courts of general jurisdiction, but federal District and Regional Courts would have exclusive jurisdiction over subject matters falling under the scope of application of federal law (international trade, federal claims) or when the dispute involves parties located in different states and a balance of over USD 50,000.



**Days Sales Outstanding (DSO):** Payments in the US normally take place within 28 days, though delays of 5 to 10 days tend to be increasingly imposed by large companies.





#### Late payment interest:

Interest may be charged up to the legal rate of interest allowed by the state in which the debtor resides.



## Getting Paid

### Days Sales Outstanding (DSO)

Payments in the US normally take place within 28 days on average, but delays of five to ten days tend to be increasingly imposed by large companies. In some instances, such as for substantial sales or special customers, terms can extend up to 90 or even 120 days.

Some businesses have begun to take a more relaxed approach to invoices. It is now not uncommon to hear of businesses that regularly extend terms without further discussion with their suppliers, and this is undoubtedly a worrying trend. Businesses are less inclined to the concept that invoices are 'due now,' not appreciating that 30-day terms or indeed any period of credit is a privilege rather than a right. Perhaps unsurprisingly, it is the larger companies that are much more likely to take advantage of their suppliers' good nature and their dependence on larger customers for trade.

### Late payment interest

Payment terms are not regulated by law and may be freely agreed upon as part of a contractual relationship.

Late payment interest may be charged to the debtor. Interest may be charged up to the legal rate of interest allowed by the state in which the debtor resides. If no such agreement is available, the creditor can charge the legal rate of interest allowed by law in that state.

### Debt collection costs

One cannot legally charge collection costs without a prior agreement signed by the debtor authorizing such charges.

Even if such an agreement exists, the courts do not always enforce it; therefore, it is best used as a negotiating tool when trying to collect a debt.

### Ownership protection

Retention of Title is very uncommon in the US, so it would not stand up in court, since secured lenders' rights take priority over the goods. UCC financing statements, being a legal form filed by a creditor in order to give notice of its interest in the personal property of the debtor to other creditors, are considered as a better alternative though it is also rarely used as debtors can normally choose another supplier that does not have such requirement.

### Payments

The most common payment methods are as follows:

The most common payment instrument in the United States is the check but, as many banks' clearing processes for international transactions is lengthy, companies increasingly tend to rely on ACH and wire transfers which are fast, secured, and supported by an increasingly developed banking network internationally and domestically. For export transactions, transfers may be guaranteed through an Export Credit Insurance policy, which helps minimize the risk of sudden or unexpected customer insolvency. Euler Hermes' worldwide network of risk offices monitors the financial well-being of customers and grants them a specific credit limit up to which clients may trade and claim should something go wrong.

Letters of credit are now very rarely used, due to the time they take to obtain and their costly nature. In light of current economic difficulties, advance payments or sight payments are preferable.

## Collecting overdues

### Amicable action

#### Negotiating

Although US courts are reliable, dealing with disputes is a time-consuming and expensive process. Hence, amicable settlement opportunities should always be considered as a serious alternative to formal legal proceedings.

Before starting legal proceedings against a debtor, assessing its assets is important as it allows verification as to whether the company is still active and whether recovery chances are at best. In addition, it is essential to be aware of the debtor's solvency status: if insolvency proceedings have been initiated, it indeed becomes impossible to enforce a debt (see below).

Legal dunning then ought to start with a registered Demand Letter recalling the debtor its obligation to pay the principal together with late payment interest. In practice, the courts often require that the parties to a dispute engage in alternative dispute resolution mechanisms in order to reduce their caseload. As a result, a majority of disputes are settled amicably and never reach the trial stage.

### Legal action

#### Ordinary proceedings

Provided that the debt is certain and undisputed, the creditor may first file an application for summary judgment. Having said this, while in theory obtaining a summary judgment ought to take nine months to one year, this is not always the case in practice. Often, the debtor's attorney would indeed ask for delays (six months to one year) so as to extend the date of the trial and to put their client in a better settlement negotiation position.

Ordinary legal action usually commences when amicable collection attempts have failed. The creditor would file a claim with the court prior to serving summons to the debtor. The latter would then be given 30 days (in most jurisdictions) to bring a defense but, if not, obtaining a default judgment could take up to one year depending on the jurisdiction and the staff available. As the US relies on discovery in order to conduct legal proceedings, the parties are normally required to provide their arguments and evidence to the opponent prior to beginning the proceedings.

The courts, at the state and federal levels alike, would normally award remedies in the form of damages, injunctions or specific performance. Punitive damages are available but remain rare in debt collection cases.

#### Necessary documents

At a minimum, the court requires a statement of account listing the amount owed to support the balance being sued for. Should the case be disputed, it would be necessary to produce the invoices, signed delivery receipts, purchase orders or any other documentation supporting the transaction. An affidavit must also be provided.

#### Time limitations

Business claims in the US must normally be brought to court between two to ten years, depending on the state where legal action is conducted. It may also be added that the timeframe for debts sold on an open account is normally shorter than when there is a contract in place.

#### Precautionary measures

Precautionary measures may help preserve the creditor's interests pending a final decision. Upon request, the courts would typically award temporary restraining orders, preliminary injunctions, or attachment orders (freezing orders are not available) as a means to preserve the status quo and to avoid irreparable damage. The claimant would however be required to demonstrate that the claim has a good chance of succeeding and that damages alone would not suffice in the absence of precautionary measures. In emergency situations, the court may make its decision *ex parte* (i.e. without the debtor being present) on a same-day basis, but the court would usually request that the claimant provides security on costs in order to protect the respondent from irresponsible action.

In practice, the courts very rarely issue such interim injunctions unless there is overwhelming evidence of fraud.

#### Lodging an appeal

Appeal proceedings may be commenced by the parties before the competent appellate courts, which would normally decline to hear the claim, confirm the judgment or request a lower court to review it. As a result, the appeal process may be time consuming. In addition, opportunities to have a judgment reviewed are limited insofar as, by contrast with most countries, appeal is only available on legal matters. At the federal level, bringing a claim before the Supreme Court requires requesting a leave from the court (*writ of certiorari*) which is rarely granted. Having said this, it is rare for debt collection cases to be appealed.

#### Enforcing court decisions

A judgment does not guarantee payment but merely gives the creditor additional rights, such as the seizure and selling of the

#### Collection @ Euler Hermes

It is always advised to attempt collection prior to any legal action in order to maximize chances of successful recovery and avoid legal costs and delays. Our key principle is to collect in close proximity to the debtor, using a series of letters, emails and phone calls in the local debtor language. Our World Collection Network of Euler Hermes offices and external providers are experts in professional trade debt collection and negotiation, ensuring positive outcomes while retaining important client relationships. Euler Hermes can handle the complete collections process from amicable, pre-legal action through to judgment and enforcement.

debtor's assets or the garnishment of their bank account. Many judgments remain unsatisfied in the United States when the debtor is judgment-proof (i.e. when there are no assets remaining from the company to satisfy the judgment).

#### How long could legal action take?

Legal action is normally a time consuming process which may last two to three years depending on the complexity of the case. The courts would not treat cases involving international parties differently than domestic claims; however the costs and delays for bringing foreign witnesses may be higher.

#### How much could this cost?

In addition to being time consuming, litigation proceedings are also costly insofar as attorney fees are significant and sometimes (to say the least) disproportionate. Cost recuperation rules would essentially depend on state regulations and contractual arrangements. Contingent no-win-no-fee arrangements, aiming at financing attorney fees through a percentage of the award in case of success, are allowed and widespread.

### Alternatives to legal action

#### Alternative Dispute Resolution methods (ADR)

Given the lengthy and costly nature of legal actions in the US, Alternative Dispute Resolution methods (such as arbitration or mediation) are very common. First, the law (under the Alternative Dispute Resolution Act, 28 U.S.C. § 651 et seq.) imposes an obligation on federal courts to provide means to settle disputes through ADR. Second and as previously mentioned, most cases in the US end through a negotiated compromise and ADR thus constitutes a relevant channel for doing so. Finally, the courts increasingly tend to order the parties to engage in a pre-trial negotiation processes prior to commencing proceedings. Some jurisdictions also consider this phase as a pre-legal requirement which, if not fulfilled, would bar access to court.

#### Foreign forums

Although unlikely because many cases tend to be collected through litigation before domestic courts, the parties could also choose to place their contractual relationship under the auspices of another jurisdiction, or of a foreign law.

In practice, state and federal courts indeed tend to uphold foreign jurisdiction provisions as long as the chosen law is reasonably related to the said contract, and that it does not contradict with public or federal policy. In addition, domestic courts would typically retain exclusive jurisdiction over specific areas of law (such as consumer protection, securities, employment, anti-trust laws) and would ensure that a foreign forum does not deprive a party from their right to benefit from a due process of law. It is however essential that the agreement be characterized by an international connection (for example, one party has elected domicile in another

country, or the place of execution is located abroad), and that a jurisdiction clause is specifically drafted for this purpose.

#### Enforcing foreign awards

Considering that each state has its own legislation, the first step in enforcing a judgment is to have it domesticated in the state where the debtor resides. Decisions rendered in one state may be executed in another state provided that the enforcing court considers itself competent to enforce, or that it had jurisdiction to deal with the claim in the first place (forum non conveniens). As a result, it is always advisable to carefully consider where legal action will be conducted, and how enforcement will take place.

In order to be considered enforceable, foreign judgments must first be recognized as domestic judgments. When bilateral or multilateral reciprocal recognition and enforcement treaties exist, this requirement is normally a formality. However, in the absence of such agreements, exequatur proceedings would aim to ensure that the enforcing tribunal did not have exclusive jurisdiction to decide on the claim, verify that the decision was rendered by a competent court, that it is final and enforceable in the issuing country, and that the parties both benefited from a due process of law. The courts, finally, would also ensure that the foreign decision does not contradict previous decisions rendered by US courts and that enforcement does not contradict public morality and public order in the US.

The United States is a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958, therefore international arbitration awards ought to be enforced fairly rapidly provided that they are final and binding in the issuing country.



#### Litigation @ Euler Hermes

Should legal action be necessary, Euler Hermes can provide support throughout the legal process from judgment to enforcement via our World Collection Network of Euler Hermes offices and external providers. Legal action can often be complicated and expensive, so you will be informed of all costs prior to any action and advised on which route is best to take.

## Handling insolvent debtors

The Uniform Commercial Code (§1-201) defines insolvent debtors as having generally ceased to pay debts in the ordinary course of business, other than as a result of bona fide dispute, or as being unable to pay debts as they become due.

Insolvency law in the US used to be considered very favorable to the debtor until 2005, when the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) made several changes to the Bankruptcy Code. Chapter 11 proceedings, indeed, have been introduced (and eventually inspired numerous pieces of legislation throughout the world) as a means to develop a rescue culture susceptible of saving viable businesses from temporary economic turmoil. Despite the changes, the bankruptcy system remains very pro-debtor and mostly rewards the administrators and attorneys that oversee the cases. In fact, it is often said that making a company insolvent is a significant way to obtain payment but in practice bankruptcy reorganization is resource-draining and only ought to be considered as the last resort after all alternatives have been exhausted.

### Insolvency proceedings

#### Out-of-Court proceedings

Although Chapter 11 proceedings aim at obtaining debt repayment through restructuring, their cost and complexity tend to make out-of-court solutions preferable prior to initiating any further action. The main out-of-court proceeding is an Assignment for the Benefit of Creditors, where a company turns over all of its assets to an independent third party, who liquidates and distributes them to all creditors in an equitable fashion.





### **Restructuring the debt**

Chapter 11 (Corporations) protection mechanisms aim to allow debtors and creditors to reorganize debt as a means to avoid liquidation. Since 2005, creditors have been given a chance to play a greater role in overlooking a debtor's reorganization: debtors have a maximum of 18 months to present a plan for reorganization and debt rescheduling. After this period, the creditors may present their own plan and submit it to the court in order to obtain approval by the creditors' committee. During the reorganization procedure, a restraining order prevents financial and trade creditors from collecting debt or enforcing decisions so as to preserve cash flows. The debtor company's management remains 'in possession' and continues to run the daily business operations, though a restructuring officer is often added to the management team. However, given that a general unsecured creditor is very far down on the list of priorities, it is very rare to see a dividend from a Chapter 11 bankruptcy in recent years. Chapter 12 (Family, Farmers or Fisherman) and Chapter 13 (Individual wage earners) provide additional reorganization options, but these are more complex.

### **Winding up proceedings**

When the debtor company cannot be rescued, Chapter 7 provides an opportunity to liquidate the debtor company's assets. In such situations, a court-appointed trustee supervises the proceedings. All creditors must then submit their claims to the trustee within ten days of publication of the bankruptcy ruling. Once the list of creditors has been established, the assets may be auctioned and the proceeds distributed among the creditors according to their priority ranking. In practice, most states protect the debtors' personal assets and there is therefore a possibility for a corporate bankruptcy to be listed as a 'no asset' case. This means that after liquidating the debts, the likelihood of any distribution to creditors is zero. Should sufficient assets be located, creditors would be notified and given time to file a proof of claim.

### **Priority rules**

Complex priority rules normally apply while distributing the proceeds to the creditors. Administrative and attorney fees would normally be considered first, followed by employee wages and benefits, federal and state taxes. Secured creditors would come next, followed by priority creditors, unsecured creditors and shareholders.

### **Cancellation of suspect transactions (clawback)**

Administrators and trustees may request the courts to cancel certain transactions concluded prior to the insolvency proceedings. In particular, any measure taken by the debtor deemed fraudulent or detrimental to the creditors would typically be void. Various suspect periods ranging from 90 days to six years may apply. Most of the time, one can negotiate when confronted with a preference action and settle the amount being claimed.

### **How long could insolvency proceedings take?**

Often, unsecured creditors could wait for two to five years or more before knowing whether or not they will be entitled to receive part of the liquidation's proceeds. Some cases have run as long as ten years.

### **Necessary documents**

A proof of claim form, statement of account, invoices and any other documents that evidence the debt.

#### **Insolvency @ Euler Hermes**

Euler Hermes works closely with debtors, creditors and lawyers to provide support during insolvency and restructuring processes. With many options available when it comes to insolvency action, we can offer advice on which option is most suitable.



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