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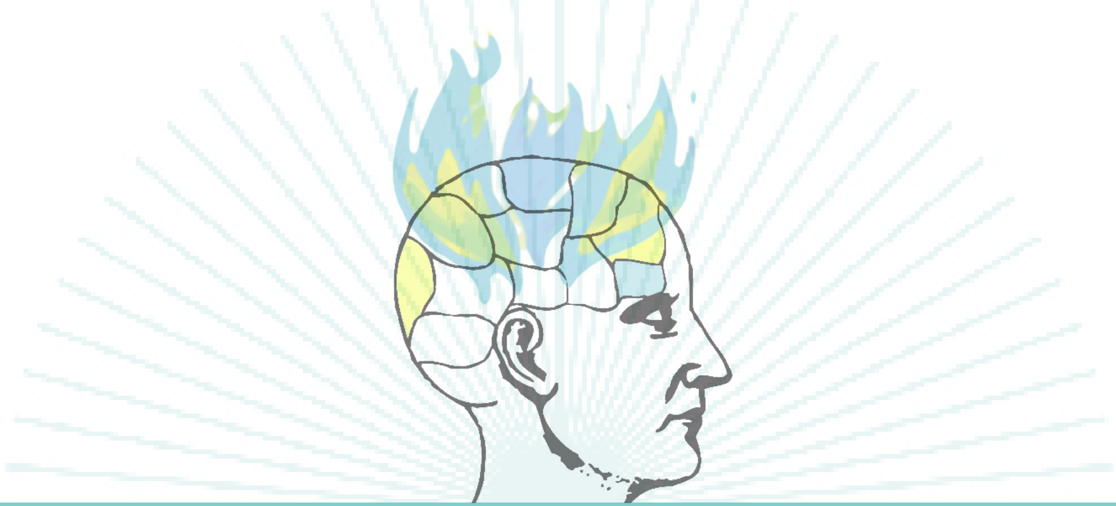
20 Cashflow questions answered

by SmartCompany experts & entrepreneurs



letter from the editor

It's the one point on which every business owner can agree – in this downturn, cashflow is the key to survival. As economic growth has slowed and spending has slowed, small and medium-sized businesses have been forced to focus more and more on cashflow – carefully forecasting their cash position, adjusting their payment terms and, of course, hassling debtors to pay their bills.

In the following eBook, SmartCompany's team of experts and entrepreneurs provide advice and tips on cashflow planning and effective budgeting, on how to construct solid contracts and set supply terms, and on ways you can encourage early payment with the clever use of discounts and incentives.

You'll also find a wealth of information on chasing up those late payers. You'll learn how to hassle, when to call in the lawyers and how you can exert pressure to ensure your bills get paid.

You'll learn about the importance of obtaining director's guarantees, the use of debt collectors and when and how you can charge interest and late payment penalties.

Cashflow management is hard work. It takes vigilance, persistence and even some outside help to make sure you get paid. But remember, there is only so much cash to go around right now and it's crucial to make sure your voice is heard.

We hope these 20 cashflow answers help you keep that cash rolling in.

Cheers, James Thomson

contents

1 I'm stressing out about my cashflow and I'm really worried about how bad things are going to get. Where do I start with this mess?

The best place to start is with some cashflow scenario planning, to find out how bad things actually are and how bad they might get. Now, this is a task that many entrepreneurs struggle with.

But forecasting is something that will improve with practice and experience – the important thing is to just start doing it.

Here are five tips for putting together a solid cashflow forecast:
1. Keep it simple: Focus first on the items that affect your cashflow most heavily, and add extras to the forecast if required.
2. Standardise: Ensure procedures for collecting and reporting cashflow data are consistent across all business units.
3. Measure your accuracy: Set the level of variance from your cashflow targets you are prepared to accept, and see how close you get each month. Where targets are missed, investigate the reasons and consider if changes are needed for next month's forecast.
4. Reward those who help: For all but the smallest businesses, putting together a cashflow forecast requires significant input from staff. Make sure they know they will be rewarded for putting in the effort to provide accurate and timely data.
5. Automate and integrate: If possible, set up business reporting and accounting systems so they provide automatic inputs into your cash-flow forecast.

Accountant and business adviser, Jan Barned

2 What do I need to monitor on an on-going basis?

This is not just a matter of watching your bank balance. You need to make sure that you can pay the bills, the wages and your loan/overdraft repayments.

Set up a system that goes forward about four weeks, and include everything that needs to be paid and all the income that you expect in that period. Obviously, the start point is your current bank balance. Use this system as a guide to alert you to any problems in the future. Don't be too fussy about getting it correct to the last dollar. As well, take into account any exceptional expenses/income that might be outside the four week period.

Check your 'average debtor days' on a regular basis. This number represents the number of days (on average) before your debtors pay up. If that average starts to get longer then you'll need to tighten your debtor control.

Most companies allow 30 days for payment. So if your average debtor days is 30, then you are doing well. If your average debtor days was 37 last year and it's now 50, then you have problems. Your customers are taking longer to pay. You can't afford to let this slip. Get on to it. You might talk to a debt collection company to ensure good procedures are in place.

If you don't know what your average debtor days is, then you'd better find out. Talk to your accountant immediately.

Gail Geronimos, founder of consultancy firm Achaeus

3 Where do I start with my long list of debtors?

Hit the phones! It's never pleasant ringing a customer and demanding payment, particularly if you are friendly with them, but unfortunately the only way to get your money is to hassle, hassle, hassle.

Start before payment is due with a quick phone call. As soon as a payment is overdue, hit the phones and start hassling. Other hassling tips include:

- Check customers have received invoices and that there are no queries.
- Deal with the same person each time you contact the company.
- Make the largest outstanding debts your priority.
- Send out statements monthly.

Greg Charlwood, Asia Pacific chief executive of debtor finance company Bibby

4 How do you deal with excuses like "Sorry, I haven't received that invoice yet," or "The cheque is in the mail"?

The use of excuses highlights why it is so important to chase debts with a call rather than a letter. If you are on the phone it's interactive and there is a lot less room to wriggle. The first question you should always ask is: "Is there any reason you have not paid this invoice?" This often gives the late-payer nowhere to go, particularly if they don't have a good reason for not coughing up.

But there has been a big rise in the number of customers disputing invoices. When this happens, try to quickly establish whether the dispute is genuine or spurious. If the problem is genuine, figure out an immediate solution.

For example, if they claim not to have received your bill, tell them you'll fax or email one immediately, or, if they are a household, tell them you'll put a copy in the post straight away. But don't just leave it at that. While you've got them on the phone, tell them the amount of the invoice and ask them whether they are able to pay immediately. It's crucial to try and get a promise out of them.

Roger Mendelson, chief executive of debt collection agency Pruska

5 What would be your advice if a debtor says they have no money to pay your account?

The first thing you must consider is the size of the debt. The options you have to pursue the debt will cost you money and therefore you must decide whether it is worth pursuing. If you determine that recouping the funds is a priority, a reputable debt collection agency will be able to assist you.

The collections agency has a range of options:
• They can negotiate with the debtor to initiate a payment plan, allowing the debt to be paid off over an agreed period of time; or
• They can seek to determine whether the debtor has assets that could be used to cover the debt.

If the debtor does have assets that could be used to cover the debt you may decide to pursue your outstanding money through the courts. However, you need to be careful to ensure that your financial interest in the debt is protected by seeking advice regarding the viability of pursuing a debtor through litigation.

And finally, ensure that you seek good advice on your specific situation – otherwise you will waste precious time and money that could be better spent in other areas of your business.

Christine Christian, chief executive of Dun & Bradstreet

6 Can I outsource debtor management?

There are a range of finance options available to small businesses that can provide an immediate boost to cashflow – at a price.

Whether called debtor factoring, invoice discounting or debtor finance, these facilities effectively allow a business to borrow against the value of their debtor book.

A debtor finance firm will come in and assess your debtor book before determining the level of finance provided, with debt facilities worth up to 90% of the book available.

An important issue to consider is whether you will retain responsibility for following up debtors for payment. Generally the smaller the client, the more likely it is the debtor financer will want to take control of the collection function. A director's guarantee to ensure payment of the debts will also be necessary sometimes.

While debtor financing isn't cheap – as well as interest, debtor financers will usually also charge a regular service fee – it is becoming increasingly common as mainstream borrowing options become harder to get and are more expensive.

James Thomson, editor, SmartCompany.com.au

7 How big does a debt need to be before I bring in the lawyers?

Every debt over $200 should be followed up with a letter threatening to bring in the lawyers.

The next step would be a tersely-worded letter from your lawyer, threatening legal action if the matter is not resolved as quickly as possible.

Stop acting like a small business. It's going to be those businesses that hassle and change that will survive through this period.

Christine Christian, chief executive of Dun & Bradstreet

8 What if my debts are bigger than $200?

For debtors who are businesses, that owe you more than $2,000 and have no valid reason for not paying, you can issue a Statutory Demand against the company.

The effect of the demand is that your customer has 21 days within which to pay your claim in full, or alternatively enter into an arrangement with you.

If your customer fails to do this you can then proceed directly to a petition to wind up that company.

It's drastic, but it's also a good way to get the cash flowing. In most companies, the threat of petition to wind up a company will need to be reported to the board, who will usually tell the accounts people to get the bill paid ASAP. It's amazing how quickly a customer will pay up when they are confronted with the prospect of their company being closed down.

Roger Mendelson, chief executive of debt collection agency Pruska

9 Should I bring in a debt collector?

This will cost you money, although most debt collection agencies operate on a no-recovery, no-fee basis – if you don't get any money back, they don't get paid. The standard charge is 25% of the amount recovered, plus GST.

There are two big benefits. Firstly, it takes the stress of debt chasing off your shoulders. Secondly, you are bringing in some professional heavy hitters who know all the hints and tricks to get cash out of people.

Anyway, a phone call from a debt collector carries much more weight than a request from your bookkeeper.

James Thomson, editor, SmartCompany.com.au

10 One of my worst late payers is also one of my biggest customers. How can I get my money without damaging the relationship?

This is one of the most common problems amongst SMEs. They just don't have the confidence to be able to chase those debts. But I think that's sticking you head in the sand.

The key to getting your money while keeping your customers onside is a professional approach. The first step is to call a meeting. If you're feeling a little nervous, take along someone to help you negotiate – your accountant might be good candidate.

Explain to your big customer that this is an important issue for you and it is having an impact on your business. Don't get too specific – they'll get the drift – but put your foot down and make your point clear. You've got to show them that you mean business.

If you can't get them to agree to pay the entire invoice, at least get them to commit to installments. To help smooth the waters, offer them discounts for early payment. The key is standing up for yourself – you'll get more respect that way.

Christine Christian, chief executive of Dun & Bradstreet

11 Can a director be held personally liable for a debt?

Firms can request that the directors of a business sign a director's guarantee – that is a secondary agreement to answer for the debt of another in case that company defaults. This contract should be drawn up by a lawyer.

Before having a director sign a guarantee, it is worthwhile investigating whether or not they have assets available to cover the debt – this can be done by running a relatively simple search such as a land titles search. Of course, there is currently no means available to confirm whether a director has signed numerous such guarantees.

Christine Christian, chief executive of Dun & Bradstreet

12 Can I put anything in my trading terms to ensure my bills are paid on time?

You need to set out your trading terms very carefully and clearly, so you and your customers know exactly where they stand. Tell customers exactly when they need to pay (for example, 14 days or 30 days), explain how they should pay (for example, by cheque, bank transfer, credit card) and clearly set out the consequences for non-payment.

The following clauses should be a part of every company's trading terms:

- A clause setting out interest charges in the event they do not pay on time.
- A retention-of-title clause, so that you have the right to enter your customer's premises and take back unpaid goods in the unfortunate event that they go into liquidation. This is known as a Romalpa Clause.
- A clause that makes the customer liable for all collection costs and legal costs (that is, these costs get added to the debt).
- A clause that prevents your customer offsetting another claim against a debt. That is, if the customer owes $4,000 but have a claim for $2,000 worth of defective goods, they must keep these two issues separate and pay the bill.
- Define the partners properly.
- A clause that specifies which state disputes will be handled in (crucial for cross-border companies).

Roger Mendelson, chief executive of debt collection agency Pruska

13 Do you have any ideas to slow the rush of money heading out the door to my supplies?

Negotiate with your creditors – just like they do with you. If possible, try to extend your payment terms (if they ask for payment within 30 days, see if you can push it to 60 or 90 days) and get some breathing space. Another option is to negotiate installment plans where possible, if only to make your cashflow scenario planning a bit easier. Otherwise, the best advice is start looking very closely at your cost base, and particularly your labour costs, which are typically the biggest part of any company's overheads.

James Thomson, editor, SmartCompany.com.au

14 Are there any ways to ease calls on my cash from the tax office?

Some businesses or investment taxpayers may have received new PAYG notices from the tax office that reflect a predicted increase of up to 6% or 8% on their income in the coming year.

For many this is nonsense, but varying the PAYG installment rate to accurately reflect likely total year income is extremely difficult in the current climate. And the threat of penalties if the variation is not substantially right doesn't help.

Forcing SMEs and others to effectively guess their income for the year in current circumstances is near-on impossible. But businesses certainly don't want to be paying more tax than they have to – cashflow is critical right now.

It all really requires a very special crystal ball to see the future right now. Your accountant or adviser can certainly help with this, but in the end, many SMEs might find themselves relying on the tax office to be understanding and compassionate about income predictions, and hence downward variations to PAYG installment rates.

Terry Hayes is the senior tax writer at Thomson Reuters

15 Can I charge late payment fees or interest on an outstanding debt?

Improving payment terms is undoubtedly a beneficial move for businesses in the current economic climate.

However, before you go ahead and implement a late payments penalty, it is important to ensure that your accounts receivable process is as efficient and effective as it could be.

An effective accounts receivable process is characterised by:
• The establishment of clear credit terms at the outset of a relationship.
• Prompt issuance of invoices.
• Tracking of accounts receivable to identify slow-paying customers.
• Regular communication with customers to identify and resolve problems before invoices are overdue.
• Action taken against a debtor if they are persistently delinquent.

If your accounts receivable process is working as it should be, and you wish to pursue the late payments penalty, there are a few things you need to consider:
• Do terms and conditions adhere with any regulation/legislation that applies to your business/industry?
• How will you communicate your new terms to your existing customers?
• This move may result in customer backlash – are you prepared to lose customers? When considering this you must remember that a persistently delinquent payer is a significant drain on internal resources – some customers are not worth having!

A late payment fee is not guaranteed to improve payment behaviour, however if it does, it will undoubtedly have a positive impact on your cashflow.

Christine Christian, chief executive of Dun & Bradstreet

16 I'd love to sleep easier at night not worrying about debtors. Is there any way to buy peace of mind?

One potential option for small businesses that are heavily reliant on a few big customers is debtor insurance. This is especially important given economic environment, where the risk of a customer becoming insolvent is increasing all the time.

Look at your debtor book and think about how important your bigger debtors are to your business. If there is one or two that would knock your business over if they didn't pay, it may be worth controlling that by insuring their payment.

It will cost you money, but it may buy you peace of mind.

Bruce Growcott, senior partner with PKF Enterprise Advisers

17 Is there a way of spotting dud payers before they become customers?

One measure that can help you avoid the duds is a standard credit check for any new client that will be offered credit. New customers could also be asked for permission to have an external credit check run on them. Credit agencies such as Dun & Bradstreet will carry out checks that provide a range of information, including a company's legal structure and credit worthiness.

At the very least, potential debtors should be asked to provide a couple of trade references. References can be helpful to determine whether a client is a 'tyre kicker' and will often tell you a bit about the credibility of the individual – as long as you actually check them.

Bruce Growcott, senior partner with PKF Enterprise Advisers

18 How can I encourage debtors to pay without heavy-handed tactics?

A tool many cash-flow advisers believe is effective, if costly, is a discount for early payment.

There are many different ways an early payment discount can work. Discounts can be scaled, so the earlier the repayment the bigger the discount, or further discounted over time for selected customers as a reward for prompt payment.

Clients should be told about discounts upfront. People often don't take up discounts even when they know about them, so if you are having trouble it is worth going back and explaining to them what they could be saving if they pay on time. That will often get their attention.

Do your research before offering a discount though. Calculate what the credit extended to customers costs your business in interest or lost opportunities, and compare that to the margin a discount will knock off your debtors book.

If a discount doesn't make financial sense, consider offering other benefits for prompt payment, such as a higher level of post-purchase service or priority access to new stock.

David Young, partner at Pitcher Partners

19 Can I get my staff to help me bring in cash from customers?

It can often be worthwhile to direct at least a portion of your sales team's commission structure towards ensuring the customers they sell to actually pay.

Small businesses with sales reps often pay commission on the amount of sales, so by swinging it around and paying a commission on sales banked, you may find that all of a sudden your sales team is in there helping you collect that money.

Staff should also be encouraged to participate in cashflow management by keeping accurate and up-to-date cashflow data and ensuring it is fed into the business's cash management system.

Accountant and business adviser, Jan Barned

20 I've got some spare cash. Do I spend or save in this environment?

Now, to get back to the question of saving or spending.

I go for the 'build your reserves' option. In other words, save as much cash as you can. We are not out of the woods yet and there is no way I'd be spending my precious cash without a damn good reason.

I know that business life is never as simplistic as that, and there are many angles to consider when making decisions, however, building your reserves should be one of your top priorities right now.

Have a serious look at your monthly P&L statements. What can you do to reduce your expenses? And be tough on yourself. Don't pussyfoot around. And do it three times so that you really cut out all the fat.

Gail Geronimos, founder of consultancy firm Achaeus

WESTPAC PROMOTION

Need more help?

Running a business in this economic climate is undoubtedly tough, so you may benefit from attending financial education and advice workshops. Westpac's interactive workshops cover a range of business financial management concepts in an easy-to-follow, practical format.

The workshops are relevant to both for-profit and not-for-profit organisations, as well as individuals, and are open to anyone - you do not have to be a Westpac customer to attend. Each workshop is presented by an experienced Westpac facilitator and can, on request, be tailored to suit a particular audience or industry.

There are a number of time friendly learning formats, so you can choose the option that best suits you.

Beyond Survival

This workshop hones in on the drivers of cash flow and profits, illustrating what financial statements really mean and ways business owners and managers can use them to their advantage every day.

- 2 x full day workshops or 5 x 3 hour bite-size workshops

Business Financial Review

Theory becomes more relevant when applied to real life. This workshops guides business owners and managers in implementing the theories learned in Beyond Survival.

- 1 x full day workshop

Business & Succession Planning

This workshop will help business owners and managers put both short and long term plans in place to maximise the value of the business and ensure transition is as easy and as profitable as possible.

- 1 x full day workshop or 2 x 3 hour bite-size workshops

Going Global

These workshops highlights the challenges faced with importing or exporting and how these may place added pressure on the cash flow cycle, offering business owners and managers practical solutions that can be implemented quickly into their operation.

- Importing: 1 x full day workshop
- Exporting: 1 x full day workshop

Key Benefits

These workshops can help you to:

- Make more confident financial decisions
- Understand the impact financial decisions will have on our cash flow and growth
- Network and share experiences with other businesses and organisations
- Learn how to plan effectively – both for short/medium and long-term
- A number of our workshops are registered with a range of professional associations and bodies, and count towards Continuing Professional Development (CPD) accreditation and subsidy eligibility
- Business education expenses are generally tax deductible (please confirm with your accountant)

For more detailed information call 1800 012 501 or visit
www.westpac.com.au/businessworkshops
or email financialeducation@westpac.com.au

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