## Debt Collection Acceleration

An article in the Australian Financial Review recently reported on a Dunn & Bradstreet finding that "firms take an average of 53.4 days to settle their accounts" and "Weak trade has hit cash flow and means many small companies are putting off paying invoices"

The article confirms what some feared would be an outcome of the recession. We are not out of danger yet, as traditionally the period after a recession is the *most sensitive* in terms of liquidations and bankruptcies.

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# Slow payers hurting small businesses

Sam McKeith

**KEY POINTS**

- Firms take an average of 53.4 days to settle their accounts.
- Weak trade has hit cash flow and means many small companies are putting off paying invoices.

More than half of all firms are being hurt by lagging payment terms as weak consumer demand, tough credit conditions, and dwindling working capital forces small and medium businesses to delay paying bills.

Data compiled by Dun & Bradstreet shows firms took an average of 53.4 days to settle their accounts during the June quarter, slightly less time than the previous quarter, but still almost a day longer than before the global financial crisis.

About 53 per cent of firms say they are feeling the effects of slow payments from debtors, a 17 per cent increase from April, according to the credit reporting agency.

The Council of Small Business Organisations of Australia said weak trade at many SMEs meant operators were putting off paying invoices.

"At many small businesses sales are down around 16 per cent, which is an absolutely huge figure and the impact on cash flow is enormous," chief executive Peter Strong said. "When you don't have the cash you've got to pick and chose who you pay the bills to, there's rent, the Tax Office, there's certain suppliers you've got to pay then there are others who won't be paid so quickly, that's reality."

SME Australia chief executive Dean Logan said continued difficulty accessing bank finance was compounding cash flow pressures at small and medium sized businesses.

Mr Logan said credit was especially scarce for businesses in the commercial property sector.

"SMEs are still catching up from the global financial crisis, they've used any residual income that they've had, any bit of fat, to tide them over that 2 year period.

"We're still trying to pick up to where we were a couple of years ago and as a result our creditors are suffering," he said.

Dun & Bradstreet said payment terms for most firms remained well outside the 30-day standard term although it noted the average payment term had shortened by more than four days since the worst of the global financial crisis.

In the three months to June micro-businesses, those with between one and five staff , posted an improvement of one day to 51.7 days. Firms with between six and 20 employees took 50.6 days to pay, 0.9 days earlier than the past quarter.

Medium-sized firms were the only group under the 50-day mark, taking 49.4 days to pay their bills.

Large firms were the slowest to settle their accounts, taking an average 56.9 days in the June quarter.

Dun & Bradstreet chief executive Christine Christian said the small improvement in the June quarter would do little to ease cash flow pressure on firms waiting to be paid.

Ms Christian said access to cash was particularly important at the moment as firms in recovery mode looked to expand their operations.

"If we are to experience the significant improvement in terms which is required to positively affect the cash flow of firms, executives need to take prompt action to collect their bills," she said.

BRI Ferrier principal Martin Green said many small business were cut off from bank finance because of Basel II capital rules that had created an incentive to lend to household market rather than to business.

"It's a killer for the banks," Mr Green said.

"The only saviour is the Tax Office; many small businesses had been funded by not paying PAYG and GST and that's allowing them to survive."

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*Leading index rises, page 5*

Slow paying customers are not new to small business. When you combine this with difficulty accessing finance you can see why many businesses are struggling to survive.

We acquire many new business clients who at first glance have lots of financial control problems. When we cut through to the core of the issue, its invariably 'Receivables' that is the problem area, where we can quickly make a big difference and find cash to help a business keep going. This provides 'breathing space' to be able to work on other areas of the business.

I would just like to share with you the 'value proposition' of spending some time, money and effort on getting Receivables under control.

If a business has turnover of **$1m** and Receivables of **$145,000**, this means they are taking **53 days**, on average, to collect payment from their customers. If the number of days can be reduced to **33**, approximately **$59,000** would come back into the bank account!

### This is precious working capital when you can't go and borrow it from the bank.

There are many steps in the process of reducing Receivables days by 20. One of the steps that can have a huge impact is following up slow payers. Business owners with 'Receivables' issues typically find this the most difficult and unpleasant aspect of being in business and lack the skills to employ and supervise someone else to do it well.  Here are some tips on this vital area of business financial survival.

**Management**

Don't allow slow paying customers to be followed up in an 'ad hoc' and reactive way when cash starts getting low.  Some ways to cement a proactive system for managing collections are

- Don't just start calling all debtors starting at the letter 'A' on the list
- Create a targeted collection campaign by segmenting your customers
    - Small dollar value invoices
    - Large dollar value invoices
- Measure effectiveness of the campaign by measuring the Accounts Receivable Days (see www.bean-talk.com for the formula to calculate this)
- Have a transparent system for monitoring collection activity – so everyone can see what's going on.
- Make <u>one</u> person responsible for managing this task.

**Efficiencies**

The key to effective customer payment handling is to do it efficiently.

- Have a strict time based system for sending reminders at pre-set intervals i.e. every seven days.
- Have standard messages depending on the age of the debt that get more assertive as an invoice ages
- Create  queues for handling
    - low dollar value amounts by email
    - high dollar value amounts by telephone
- Keep good records of telephone conversations and commitments made by debtors.
- Schedule next actions and send reminders to those involved i.e. other team members
- Have a system for escalating problem debtors to management
- Identify disputes and handle them quickly
- Identify invoice errors and handle them quickly

**Team Work**

It's often left up to one person to chase payment, but if everyone gets involved where they should, issues get handled more quickly

- Get all staff involved to allow speedy resolutions to issues
- Send reminders to team members to do actions agreed

**Cash Flow**

Well managed and efficient debt collection will have a hugely positive impact on cash flow

- Measure the impact by predicting your percentage confidence of collecting debts and the date you expect to collect payment
- Getting the money in quicker reduces the need to borrow for working capital
  - Reduces interest costs
  - Increases interest earned on positive bank balance
  - Saves money spent on staff time to collect inefficiently
  - Reduces likelihood of bad debts – the longer a debt is unpaid the more likely is will turn ‘bad’

Consistency is the key to good debt collection. The minute you slip, customers lapse back into slow payment.

Not many Small Businesses have expertise in this field, but take heart, there is a great system available to help with the lion’s share of this work – it’s called Cash Flow Builder. It’s available from CFO On-Call – call us for a FREE demo and calculation of the possible improvement in your bank balance today. It costs a fraction of $59,000!!!

Sue Hirst is a director of CAD Partners Pty Ltd which operates CFO On-Call, a team of Financial Controllers who can help business owners understand the ‘Cash-flow Cycle’ and grow business safely. Phone 1300 36 24 36 or 0800 180 400 for a free copy of their booklet How to control your business cash-flow…and keep some for yourself. www.cadpartners.biz