

strategy guide



# Improve your cashflow by paying expenses more slowly

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## A. Introduction

- » Learn how paying expenses more slowly increases your cash flow.
- » Discover the different method for paying accounts more slowly,
- » Identify how to systemize the process to maximize efficiency.

## B. About paying expenses more slowly

Naturally, the slower you pay your debts (within the terms between you and a supplier, of course), the longer you get to keep cash in your pocket. In other words, the healthier your cash flow is. And the healthier your cash flow is, the more easily you can manage your business.

If you're in retail or hospitality you naturally deal mainly in cash so there's a very good chance you don't have a debtors' problem.

On the other hand, in consulting or professional service businesses you often don't receive payment for the work for months after you have completed the job. Yet, at the same time you have fixed variable overheads to meet.



That's why forecasting your cash flow is very important. It prevents you from landing in hot water by creating too large a gap between cash inflows and cash outflows.

As you are probably aware, a cash flow forecast or budget is a financial statement which shows the cash position of your business based on various income and payment activities that need to happen over a period of time.

A number of variables are also factored in, including what happens if sales increase or prices increase over a period of time etc.

There are a number of reasons why a cash flow projection is so vitally important:

1. It ensures you don't spend more cash than you have.
2. It predicts when you will have surplus cash which you can then use to invest.
3. It helps you forecast the likely outcome of various initiatives that you have planned so you can see the likely affect on cash flow before you make a decision to commit.



Cash Flow Projections are particularly useful in identifying, planning for:

- » short or long term **financing needs**
- » seasonal **business fluctuations** which need to be financed
- » **debt reductions**
- » **capital expenditure** (equipment purchases)
- » taking advantage of **cash discounts**
- » **inventory purchases**
- » increasing your **investment income**

Once you have a good grasp of what your cash flow forecasts are, it's naturally very important to then manage your cash flow on an ongoing basis. In other words, put in place strategies to increase your cash inflow and reduce your cash outflow at any given time.

- » Develop monthly, quarterly, 6 monthly and yearly cash flow forecasts
- » Develop 3 Forecasts – optimistic, pessimistic and realistic and develop contingencies for each.



## The Answers

Fundamentally, there are 6 broadly grouped categories to improve cash flow:

1. Increase sales.
2. Increase the speed at which you receive payment.
3. Reduce the speed at which you pay expenses.
4. Reduce the amount you spend.
5. Sell off assets.
6. Arrange external finance.



## C. How to pay slower

Inside this Study Guide we're looking at no. 3 – reduce the speed at which you pay expenses. Here are the strategies to do that ...

### 1. Slow down accounts payable

Obviously, you need to pay your bills if you want to maintain a good credit rating AND if you want to maintain a great relationship with suppliers.

Having said that, never pay your bills early. Always pay them ON the due date – unless you receive a discount for paying early, that is. Even a 1% - 2% discount puts more money in your pocket so take advantage of it.

In situations where you are struggling to pay bills on time, there are some simple steps you can put in place to get your business back on track.

They are:

- » Extend the credit limit. If you have a good track record with a supplier most will oblige (see next point).
- » Split Payments – ask if you can pay your account in thirds over a 90 day period without interest penalties.
- » Credit Card with interest-free period (see later in this document)
- » Keep the Accounts Payable contact information = stay in contact with the accounts payable person and let them know your situation and come up with ideas on how the situation can be resolved. The supplier wants their money so they will often be flexible. If they can't simply take your business elsewhere.

### 2. Renegotiate payment terms with suppliers

Naturally, purchasing from a supplier on credit is a valuable source of cash flow for your business. It's like an interest-free loan assuming you pay before the due date.

Payment terms can vary from 7 days to 30 or 60 days or in some situations, even 90 days.

If you can negotiate a way to pay your creditors in 60 – 90 days and get your debtors to pay in 30 days, your cash flow will dramatically improve ... naturally.

Some suppliers will be willing to negotiate better payment terms if you have a good track record of payment with them and your business is of great value to them.

In many situations, if you have a proven track record of paying on time, your supplier would rather extend these payment timeframes than lose you as a client.



When it comes to payment, remember to pay your accounts ON the due date, and not before. After all, it's much better to have the money in your pocket and not someone else's.

Electronic transfers and BPay are a godsend for automating the bill payment functions so suppliers can get paid on time, every time (not early and not late) without worrying about writing and sending cheques then having them arrive early or late.



## Exercise:

1. Sit down with your accounts payable people and identify the payment terms that suppliers are currently offering.
2. Notice how quickly you are currently paying invoices in relation to their payment terms.
3. Identify a list of suppliers you can approach to extend the time frames.
4. Approach them.
5. Develop a new accounts payable system that makes it easy for you to pay ON the due date and not before.
6. Can you start using electronic banking instead of writing cheques?
7. Can you use a 55 day interest-free credit card to make payments to extend your credit period by a further 55 days?

### 3. Pay your people fortnightly or monthly

If you're paying your people weekly, change that to fortnightly or monthly and you'll find that has a massive impact on your cash flow.

Not only that, it will also reduce your payroll administration costs by 20 – 50%. This time saving can then be used in other areas like debt collection.



### 4. Change suppliers

In an ideal world we could all stay with the same suppliers year after year and enjoy a great working relationship. In any cases this is possible but it's important to (at the very least) be aware of what other suppliers are offering in comparison.

If your existing supplier doesn't offer you the payment flexibility, quality and range you're looking for, maybe it's time to renegotiate OR look around for other alternatives that offer you a better deal.

The list of supplier "must haves" are:

- » The right value –for-money on offer – great price in relation to the quality of the product.
- » Ability to pay slowly but receive immediate access to the product.
- » Good delivery times, flexibility and customer service (naturally).

For most businesses, the ideal scenario is to stay with their current supplier but to enjoy better terms and conditions so always negotiate with your current providers first. Before you do that though, be aware of some alternatives out in the marketplace so you know where else you can go if those negotiations fail.

### 5. Ensure sales commissions are based on money banked not money billed

Many businesses make the mistake of paying sales people on the amounts they invoice not the money that actually gets banked, In situations where customers don't pay or take months to pay, you are financing your sales people's commissions which can cause a huge cash flow drain.

Instead, if sales people know they're only getting paid when you receive the money, they'll pay much more attention to qualifying buyers, maximizing customer satisfaction and encouraging customers to pay quickly.

This initiative in itself will have a dramatic impact on your results.

At face value, this may sound like it won't make a big difference to cashflow, but when you check out this example I think you'll be quite surprised.



Let's say that each of your salespeople have targets of, say, \$80,000 per month, each. You have 4 salespeople and for simplicity, that equates to \$320,000 in sales they need to generate. They're great sales people so they do make their targets.

The way in which they record their sales though is once someone signs a purchase order they're considered to be a sale (in the eyes of the sales person). The trouble is, the timeframe between the purchaser supplying a purchase order and the money getting paid is approximately 60 days.

So – let's say that you're paying your sales people 10% commission. When they record a sale in June they're currently getting paid in June but the client isn't paying until August. That's \$32,000 you need to find in June, from money you don't receive until August – a whopping 10% of revenue that hasn't actually been earned yet.

If you had \$32,000 in the Bank for 2 months @ 5% pa interest, that's \$266 in interest you could have earned. May not sound like much but it all adds up. In fact, spread that over a year and that's \$3192 you're throwing away.

Worse still, if you need to eat into your overdraft to pay your team members these “future commissions” how much interest are you paying unnecessarily?

Starts adding up, doesn't it?

Then – factor in that 10% of clients (you may find that it's actually more) change their minds before they pay, \$3200 of that money is a loan you're giving out to our employees for a two month period – commissions that you're paying now, that they'll need to pay back when the customer changes their mind and decides NOT to purchase. Not only does that make for an unnecessary drain on your cash flow, it is also “messy” and time consuming to administer as well.

### Exercise

1. If you don't currently produce cash flow forecasts, start doing that now (Refer Study Guide). When you do that, notice the difference that paying sales commissions on actual money banked, makes to your cash flow.
2. In conjunction with your accounts people, develop a new system for monitoring and paying sales commissions using this technique.



## 6. Use a company credit card with an interest-free period

Company credit cards with extended interest-free periods are a fantastic way to free up your cash flow without costing your company money in interest.

So – do your homework and find the credit card company that offers the most inviting terms and conditions possible. The longer the interest-free period is the better.

Many financial institutions have credit cards with 55 interest-free periods. Using these types of credit cards enables you to purchase something now and pay it back within 55 days without being charged any interest on the purchase. Then – if the credit card also has frequent flyer points or other loyalty rewards, not only is it costing you nothing, you're also earning money on every purchase you make.

Having said that, it becomes vital that you pay your credit card on time. If you don't you're costing yourself big dollars in interest.

To maximize the benefit of paying by credit card, it's obviously important to use suppliers that accept payment by credit card. It's also important to watch your spending habits so that you know where you're spending money.

One more thing – contact your financial institution and synchronise the billing cycle with the due dates on your supplier invoices. That way you have the full 55 day interest period to pay your accounts.

So – on a 60 day supplier account, you could pay their invoice on time and then have a further 55 days to pay off your credit card. This gives you 115 days of credit. This can make a massive difference to your cash flow.



### Exercise:

1. Review your current company credit card interest-free period and loyalty scheme. See what else is being offered in the marketplace. Find the card company that offers the best interest-free period with the best rewards scheme and apply for a new credit card.
2. Contact your suppliers and see if they accept credit card payments.
3. See if you can synchronise billing cycles between your suppliers and the credit card companies to take advantage of the entire interest-free period.



## 7. Implement a payment system

The effectiveness of the accounts payable strategies mentioned in this guide all boil down to your ability to systemise the payment process so it happens efficiently within the timeframes recommended.

If you don't, you will be penalised by your suppliers AND you will incur interest charges from your credit card provider and/or supplier.

So - without a system that schedules payments for their due dates and manages your cashflow, you will find yourself struggling to stay in control of your finances.

To solve that problem arrange for your accounts payable person to develop a system that allows you to track and approve all money that is going out of your business.

These are all manner of systems you can develop however it doesn't need to be elaborate. It might be as simple as having an expanding file which records which bills need to be paid when.

No matter which payment system you develop it's important that it has the following:

- » It is automated and ongoing and it is SIMPLE
- » Everyone that is involved with accounts knows how to use it properly without making errors
- » It produces the right amount of information to get accounts paid without being penalised because it is overdue.
- » It enables you to diarise for payment ON the due date NOT before so your money can be best utilised where it is needed.
- » Allows for time lags involved in getting payments approved, cheques authorised and posted in time to meet deadlines.





## 8. Re-asses your accounting system

Today, virtually all businesses have their own computerised accounting system. Having said that, not all of them function efficiently.

Here is a list of features that will maximise the efficiency of your system

- » Easy data entry and reports
- » Electronic Bank Reconciliation
- » Budget setting, tracking and progress statements
- » Pay bills easily and have them tracked and recorded
- » Do quotes
- » Track the progress of projects
- » Entry of timesheets and staff expenses
- » A variety of reports
- » Customise letterhead for statements
- » Multiple user functionality
- » Import bank statements from the internet and reconcile transactions to minimize manual entry.
- » Invoicing flexibility – change columns, descriptions, payment terms, payment methods easily.



## D. Key points summarised

- » Pay expenses more slowly to increase your cash flow.
- » Utilise different methods for paying accounts more slowly,
- » Systemise the process to maximise efficiency.

## E. Action steps

What	Why	Who	When
Prepare updated cash flow statement and projections	Understand where your business is at financially	Your accounts person	
Brainstorm ideas with your accounts people and purchasing people, on how to pay slower	Generates even more ideas from people who deal with suppliers at all different levels	You, your accounts people and your purchasing officers	
Prioritise the ideas and draw up an action list	Ensures you address the tactics that will generate the best return for the least effort	Your key people	
Amend the cash flow projections to determine the impact these strategies will have on your cash flow	Identify how your cash flow will be improved by implementing the ideas	Accounts person	
Implement strategies and monitor results	See cash flow improve	Your accounts people	
Ask your 10x Coach	Review cash flow projections and “pay slower” strategies to identify any challenges and advise on additional ideas	You and your 10x Coach	

