

Chapter 2

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The Basics

Typically, when you hear a discussion about cashflow and how to get it under control, there are three areas of your business that are covered:

- Collections
- Disbursements
- Waste

Collections involve getting your customers to pay you what they owe, when they owe it. **Disbursements** are payments to your vendors for products or services. And remember when your parents told you to turn out the lights when you left a room? Well, that sort of thing would fall under the **waste** category.

Now, if you're thinking this sounds rather straightforward, you're right! That's why it's called *basic cashflow*. If you think you've already got the basics mastered, you can either scan the next few pages (just in case they invented something new while you weren't looking) or you can flip ahead to the next chapter. The basics will still be right here should you ever need to refer to them in the future.

Collecting What You've Earned

If you hope to have any success with collections, you really need to have a written credit policy. By a written policy, I don't mean you need a long formal policy that no one wants to read. It can be very simple:

Upon management approval, customers are authorized to make purchases on account. Purchases are to be paid within 30 days from the invoice date. Unpaid balances incur a monthly \$15.00 late fee. An unpaid balance which is 6 months or more past due, will result in termination of the customer's ability to make purchases on account. The company will pursue all legal means to recover payment.

Then, once you have a written policy, you need to enforce it.

You mean everyone won't automatically follow the policy?

Let's say you offer a 2% discount if the invoice is paid in 10 days. XYZ Company always deducts 2% but their check consistently arrives 15 days after the invoice date. That's **5 days** past the discount policy due date! You've wondered if you should say anything to them, or charge back the discount deducted inappropriately, but you definitely don't want to offend them. They are a good customer, after all (note to self: check definition of *good customer*).

But now their payments are arriving close to 20 days after the invoice date and they still deduct the early payment discount. Where do you draw the line? Enforcing your credit policy helps you avoid awkward situations like this with your customers.

So, what might you want to do about XYZ Company? A couple of options are:

- 1) Be honest. Call them and state the facts. Say, *"Your last payment arrived 20 days after the invoice date and included the discount for payment in 10 days. I know in the past we've given you a little bit of a grace period. But I wanted to let you know that going forward we won't be able to do that."*
- 2) Change your credit policy to 2.5% discount if paid in 10 days from the date of invoice. This gives you a chance to enforce a "new" credit policy. You'll want to make it clear

to customers their payment must be *received* 10 days from the invoice date to take advantage of this higher discount rate. No exceptions.

As with most things in life, if we know the rules of the game, it's more likely we'll play by those rules.

Of course, in any situation, the customer has a much more difficult time paying you by any due date if they don't have an invoice.

The longer you delay in billing your customer, the longer you are extending the collateral-free loan.

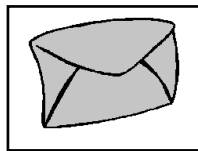
It's just good business sense to issue an invoice immediately after the sale or service you perform.

Wait a minute! Did I just say *collateral-free loan*?

Exactly.

Just in case you didn't realize it, that's what you do each time a customer buys from you on credit—you are extending a loan without requiring any collateral.

This is unlike when you get an auto loan and the bank holds title to your car as collateral for your loan. To top it off, the collateral-free loan you extend to your customer is often extended interest free! Your bank doesn't even give you an interest free auto loan.



When sending the invoice to your customer, you may want to include a self addressed envelope to encourage prompt payment. Of course, if your customers are large corporations who issue computer generated checks, they probably already have window envelopes which match up perfectly with their checks and would only pitch your self addressed envelope in the circular file.

On the other hand, if your customer is one who can be encouraged to pay more promptly because of a little convenience offered on your part, I'd go for it. You already have the history to show how long it takes your customers to pay you when you don't send a self addressed envelope. Now, keep track for the next few months to see if the payment time improves at all with this new approach. Make a note 3 months out to review your customers' payment history to see if the self addressed envelope had a positive impact on your cashflow.

OK, so we've sent out the invoices. Now, when you get those payments in the mail, what do you do with them? Put them in a drawer and wait till you have a week's worth to deposit?

Absolutely not!

Make your deposits immediately! By delaying the deposit, you only extend the collateral-free loan you've given the customer.

What if your customer wrote a number of checks and there's a chance they won't have the funds to cover them all? You want to get your check to the bank first to increase your chances of collecting the money.

If you have to collect on a check that doesn't clear, or worse, a past due invoice, what do you do? Your best bet is persistence. Sorry, there's no other magic pill than that. I suggest the following:



- First, put a smile on your face for that "I want to keep you as a customer" sound. A smile adds warmth to your voice and customers can hear that.
- Second, ask about their business with genuine interest. Is it good, slow, or ...?

- Third, ask when you can expect payment.
- Finally, makes notes about your conversation.

This last step could be critical if there is a *next* call (and believe me, there will be *next* calls). Should their check not arrive as promised, make another call to your client (don't forget to smile). Using your notes from the previous call as a memory jogger, you can refer to specifics such as:

- the status of check #29452 which was sitting on their desk when you last talked, just about to go in the mail, or
- the big contract with ABC Automotive Company they were expecting to land which would give them enough cashflow to pay on their account.

Your call with these specifics demonstrates that you pay attention to what they tell you and your call to them will occur like clockwork unless you receive payment.

You'll be known as the squeaky, but pleasant, wheel. If your perpetually cheerful voice isn't enough to make you memorable, your persistence will. And the only way they can stop you from calling to ask for payment, is to pay you.

Timing Cash Disbursements For Maximum Results

The cash you've worked so hard to earn (and sometimes collect) is not something you want to part with easily. You want to pay your bills when they're due, but not a second before. Paying your bills as they arrive isn't a very efficient way to handle that process in your business.

**As with each part of your business,
you need a system for paying your
bills that works for you and
manages your cashflow.**

Whether you use a program such as Quicken or a simple spreadsheet or the back of an envelope, you need a way to see what payments are due in the next week, the week after that and the next month.

Your list should include your upcoming bills and their due dates. Then, when you sit down once a week to make payments, you know at a glance how much those payments add up to. By consistently maintaining this list, you will know how much cash you're going to need next week and each week thereafter. And your history of consistently paying on time will pay off for you later if you get in a cash crunch and need to request a grace period.

One way to help even out your payments is to order your stock more often, and in smaller quantities. This helps your cashflow in two ways:

- Your payments to your vendor will be spread out more evenly (hopefully a little closer to the way your cash will come in)
- Each payment will be smaller since you purchased lower quantities than if you had purchased a whole month's supply at once

Reducing Waste

Keeping less stock on hand at any one time can help in other ways. The more inventory you carry, the easier it is for some of it to *shrink* or disappear. That could mean some of it was put in a separate storage room because when a month's worth was ordered, it wouldn't all fit in the normal storage area. Near the end of the month when you should still have had some inventory, no one remembered that some of it was stuffed into the top of the janitor's closet at the end of the hall.

But *shrink* can also mean the inventory walks out the door without a sale occurring. Obviously, not good! However the inventory shrinks, it is more likely to happen when you have *more* (or

perhaps too much) inventory. Who will notice if some is missing? Keeping less inventory makes it more obvious when inventory is missing.

Monitoring all your processes for more efficient, less costly ways of operating is the key to reducing waste.

Often, operations people have the best ideas to help reduce waste because they see opportunities every day. They've probably already thought, "*Yeah, if this were my business, I'd sure do it differently.*"

We all like to be asked for our opinion and your staff is no different. Think of the potential chain of events: asking your staff for ideas, using their ideas to make productivity improvements or eliminate waste, and sharing a percentage of the savings. Oh my, where might it lead?! Improved morale, improved productivity, improved profits...

Limitations Of The Basics

So, now that you've got the hang of the basics of cashflow management for collections, disbursements and waste, what's next?

Once you have a credit policy in place which you're able to enforce with most customers and you have a system in place for minimizing past due invoices, what should you focus on next?

Once your disbursements are set up with a system to maximize timing, what then?

And balancing efforts with results can only go so far with waste reduction. Your efforts at waste reduction should have targeted the biggest chunks of your expense. Any further efforts at reduction would likely be more effort than results.

So, once you have your collections, disbursements and waste under control, what else can you do to increase your cashflow?

Are you looking for more ideas to add cha-ching to your small business? Are you looking for ideas that will bring in more sales, ideas that involve no cost or low cost? Are you looking for ideas for planning and managing that will have a positive impact on your business? Then, the following chapters are for you!

Key BIG RESULTS Points:

1. A credit policy – you need to have one – you need to enforce it.
2. Know how much cash you need this week and each week thereafter.
3. Monitor your operations for opportunities to reduce waste – your staff may have the best ideas.

Your BIG RESULTS Action Steps:

Record actions you can take now to get BIG RESULTS.

“Do it big or stay in bed.”
-Larry Kelly

