

Maryland Entrepreneur Quarterly

CASH FLOW IS KING



By: Marc Rubin

Growing companies fold. Profitable companies get sued for not paying their bills. Innovative companies can't make payroll. How can this be?

They simply lack control over their cash flow.

Although showing a profit on paper is very important, for small or growing businesses the most critical measure is often cash flow. It determines whether or not they can pay their most important people – their vendors and personnel. There are numerous ways to improve cash flow in your business, and they can be broadly classified in two ways: cash coming in and cash going out. Below are some tips for both.

Cash Inflows

Get Paid Quicker

- Obtain a deposit when the order/contract is written.
- Offer terms of "2/10, net 30". This means that you will give the customer a 2% discount for paying within

10 days; otherwise, the net balance is due within 30 days. The implied interest of these terms is about 45% per year – that is, if your customer does not take advantage of the early payment, he is effectively taking a loan at 45% per year to pay at 30 days! If he does the math, he'll likely pay early.

- Issue invoices promptly. Ideally, issue your invoices with the delivery of your product/service.
- Clearly indicate on the invoice when payment is due. Customers will delay payment as long as they can. It's your job to let them know that slow payment is a problem.
- Send self-addressed, stamped, remittance envelopes with your invoices to save your customer time and effort in paying you.
- Charge interest for slow payment. Of course, you might alienate customers by doing this, so choose wisely. However, you should at least maintain it as an option and include an interest provision in your terms and

conditions. If you ultimately go to court for nonpayment, you'll want the ability to recover interest.

- Promptly deposit checks. Also, if your business processes hundreds of checks per day, consider "remote deposit" with your bank, where you simply scan the check and the deposit is automatically transferred to the bank without anyone leaving your office.
- Accept credit cards. Although there are associated fees, you get paid much more quickly.
- Sell old inventory at a discount for a quick cash influx and to minimize holding costs.

Minimize Bad Debt

- Run credit checks on new clients and call several business references.
- Closely monitor accounts receivable and don't allow small problems to turn into huge problems. Require slow payers to pay up front in the future.
- Refuse future orders when bills remain unpaid.

CASH FLOW IS KING

- At a minimum, establish payment plans for slow payers – small payments are better than no payments.
- Whether in-house or outsourced, establish collection procedures and stick to them. You're not a bank – don't let customers treat you like one by giving themselves loans with your receivables.

Cash Outflows

Pay More Slowly

- If payment terms are 30 days, don't pay the bill before that, unless you're offered terms of 2/10, net 30 (see above).
- If you have subcontractors or vendors, try to pay them only after you've been paid by the client. This may require some negotiation on your part.
- Use electronic funds transfer to pay at the latest time, without worrying about a check getting lost in the mail.

Minimize Expenses

- When choosing vendors, understand that sometimes

better payment terms and discounts are better than a lower price.

- Minimize inventory and adopt just-in-time practices. Every day that an item sits on your shelf costs you money. Conversely, if your inventory is short and you have to incur shipping fees and other higher costs to meet a customer's need, that will also sap your cash. Analyze your inventory to find the optimal level.
- In addition to looking at profit margin when choosing which products/services to sell, remember to look at turnover – how quickly you can sell those items and get paid. Some high-profit items might take six months to get paid, which can be the death knell for many companies. But a slightly lower margin product might yield much quicker payment.
- Reconcile bank statements each month and ensure there are no mistakes.
- Analyze credit-card processing fees. That industry is very complicated, with

dozens of hidden and hard-to-understand fees. Bottom line: divide your total credit card expenses by your total credit card sales. If the amount exceeds 3.5%, you're probably paying too much.

Prepare for Surprises

- Build a cushion of accessible cash.
- Establish a line of credit.
- By all means, when you find yourself in a cash crunch, stay in touch with your vendors and subcontractors. Explain what's happening, tell them you're focused on getting them paid, and advise them when you will be able to pay. Suppliers will rarely take you to collections if you maintain open communication.

Marc Rubin, CPA, CVA is Managing Partner of Berman, Goldman & Ribakow in Ellicott City, Maryland. He can be reached at 410-418-4400 or MRubin@bgrllp.com.