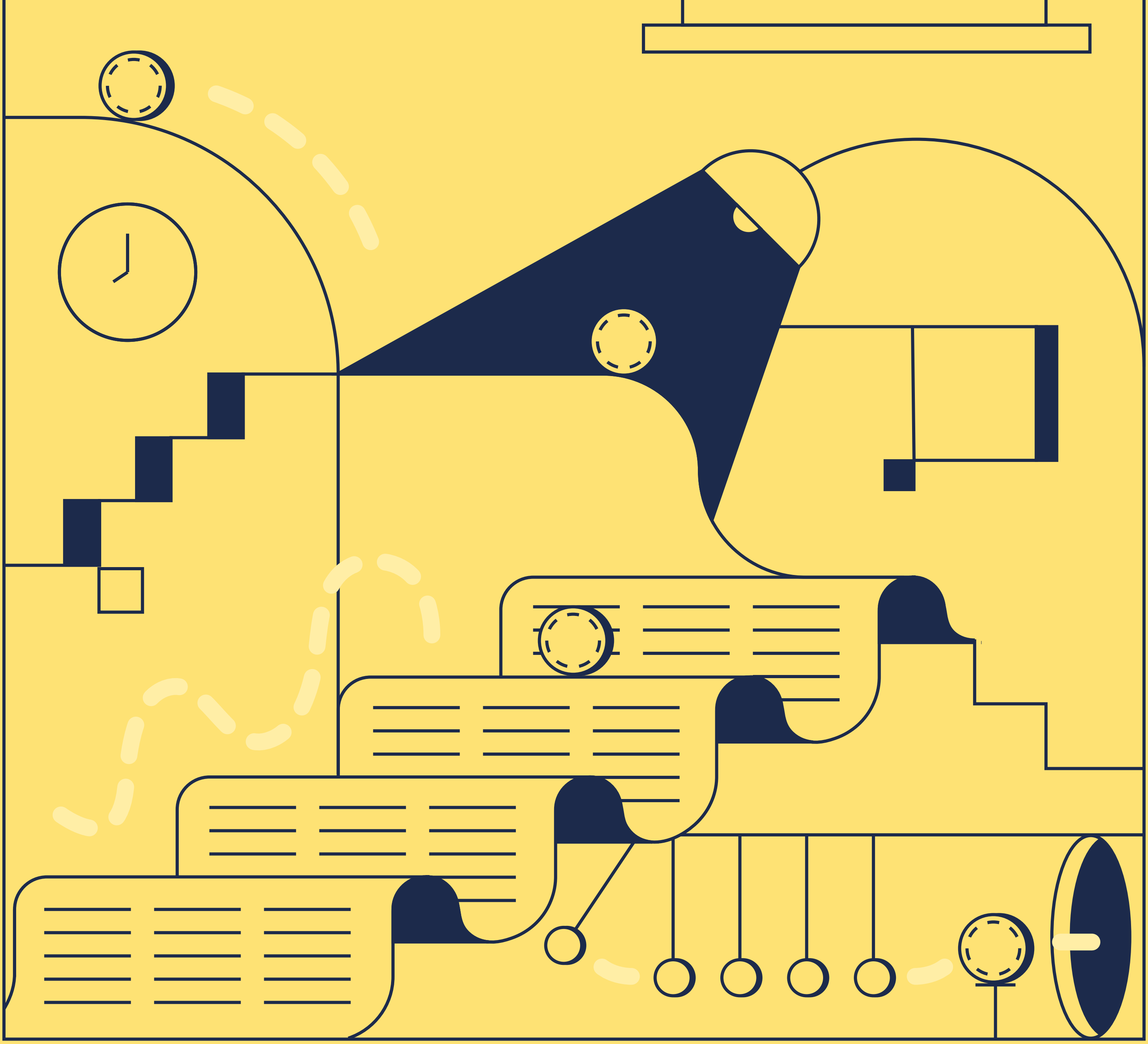
GOCARDLESS

The complete guide to optimising your accounts receivable



Introduction

Everything rests on cash flow

Managing cash flow might seem like something that only small businesses worry about. Surely, when a company reaches a certain size, it becomes strong enough to weather the storms of fluctuating cash flow levels.

But maintaining strong cash flow is a key priority for any business, regardless of its size. Large companies might not run out of cash as quick as smaller organisations, but poor cash flow can stop even the biggest businesses from making the investments they need to grow.

As a finance leader, you're used to managing risk on a daily basis; which should include managing the specific risks that cash flow problems pose to your company. This guide will help you improve your accounts receivable function, the effectiveness of which is tied directly to the health of your overall cash flow.

What does accounts receivable mean, exactly?

In an ideal world, all clients would pay their invoices immediately after receiving them, ideally by some form of online instant payment. That may be the case for some of your invoices, but it's becoming the norm for clients to stretch the payment window to greater and greater lengths to suit their own cash flow needs, especially when the client in question is a business bigger than your own.

Accounts receivable are, in effect, loans made to your clients by your company. The client promises to pay the outstanding balance by a certain date.

The average payment terms for a UK business is 24 days, but the average debtor days is 58 days, meaning a gap of 34 days of payment delays.

Offering these 'loans' can work for your business, but problems arise when they fail to keep this promise.

Implementing an effective accounts receivable process for your company goes a long way towards helping you manage and reduce the risk of cash flow problems.

Of course, no company intends to implement a weak or badly managed accounts receivable process. In most cases, it's just something that happens, either through poor planning, poor enforcement, lack of resource or failure to keep a firm enough eye on the end goal.

Neglecting your accounts receivable process risks placing your firm on a precarious cash flow knife edge, where it won't take much to push it over.

According to Business Insider, 82% of businesses that fail suffer from cash flow problems at some point, and 29% directly fail because they run out of cash.

What this guide will cover

By optimising your cash flow through a stronger accounts receivable process, you're not only putting your business on a more stable financial footing, you can also free up working capital to invest in activities that will push your company ahead of the competition, such as pursuing growth strategies, developing your employees, and maximising shareholder returns.

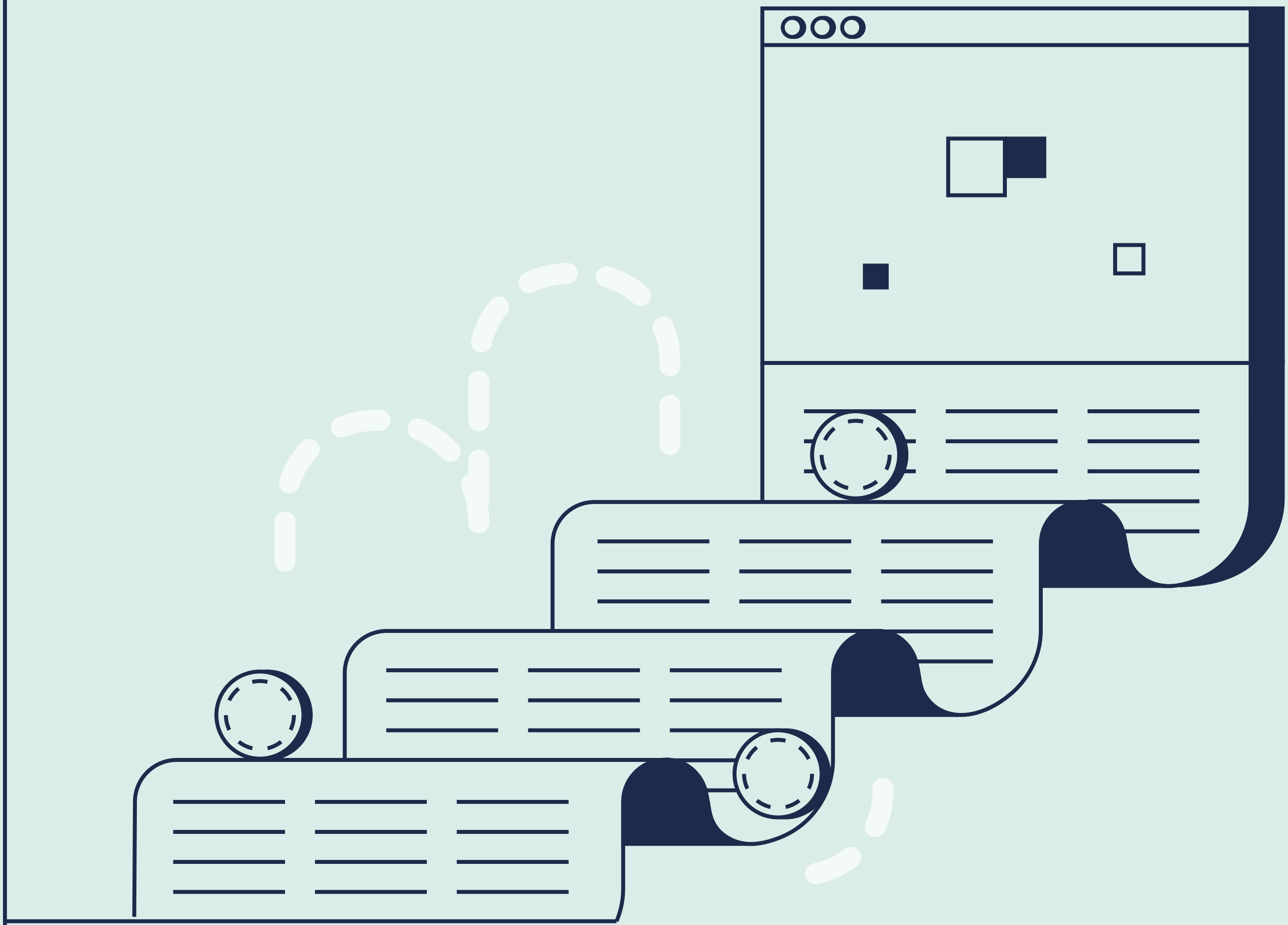
In this guide, we'll walk you through a number of ways to optimise your firm's accounts receivable process.

Optimisation can be thought of in two main areas:

Optimising your process	Optimising your clients

We'll delve into each of these areas in turn, providing actionable steps that you can put into place right away to bring visible improvements to your firm's cash flow.

Optimise your process



Let's begin by considering the area over which you have the most control: your firm's existing accounts receivable process. For starters, let's take a look at some common elements of the process that often let down a company's overall approach to collecting payments.

Define your objectives and KPIs

Before adding any potential improvements to your process, it's important to define the objectives in the form of KPIs. These can be added to your standard revenue and profit tracking reports, to provide a complete picture of your cash flow situation.

The most common measure of accounts receivable is debtor days (sometimes referred to as days sales outstanding). The typical number for a UK business is between 24 days, but anywhere from 15 to 60 can be considered normal.

But, ideally, it should be as low as possible.

Debtor days is the average number of days required for a company to receive payment from its customers, which it has issued invoices to.

"What gets measured gets improved"

Peter Drucker

Debtor days has a significant impact on cash flow, so it should be among your most important key metrics when planning an accounts receivable strategy.

Reducing debtor days should be one of your key goals because a bigger number means that your firm requires an increased level of cash flow. If your company doesn't receive the expected levels of cash from accounts receivable, then it may have to resort to other methods to get capital, which could mean delaying accounts payable (creating more of the same issue for your other suppliers), or taking out a loan from the bank.

All of these options increase risk and should be avoided if possible.

You can select which metrics best fit your firm's specific needs and use that as the starting point for your optimisation strategy. Optimising each of these metric involves reducing them to the lowest possible amount.

After defining the key metrics, let's now look at the most important steps for tightening up your accounts receivable process.

Other useful metrics include

The percentage of late-paying clients	The monthly percentage of write-offs	
Aged debts (amount of overdue debt at the end of month/year)	The number of follow up collection calls made	The number of reminders generated

Keep your credit close and review your policies

“It pays to have a clear policy”

With accounts receivable being, in effect, a way of lending to your clients, it pays to have a clear policy for defining exactly who gets credit, how much they get, and how you plan to recover the debt.

This process will be made easier when the sales and finance teams work together to share insights on what makes the most sense for your specific client base.

In your policy, it’s important to set out the precise circumstances when credit limits can be overridden or accounts placed on hold.

Also, the policy should define when to assess client credit limits and should be reviewed on a regular basis to make sure it’s still relevant to changing business circumstances.

Get your data right (and keep it up to date)

Your billing and collection system should include detailed information on each client, including payment terms, credit limits and discounts, along with other details such as delivery address and email address.

With large databases, in particular, there’s always the risk of inaccuracies creeping in and causing problems. Something as simple as a client email address being incorrect can cause delays in accounts receivable because the client never received the invoice in the first place.

Never just assume that the client database is 100% correct. Regular checks and comprehensive training for anyone involved in inputting information into the system are required to consistently maintain data accuracy.

Streamline your invoicing workflow

Despite invoicing being so central to business success, a surprising number of companies slip up when it comes to devising an efficient, error-free workflow.

Issues can range from getting client information wrong on the invoice, to failing to generate an invoice in good time or even forgetting to do so at all.

Take a look at our handy invoicing templates to make sure your requests for payment include all the necessary information.

Many companies invoice their debtors in batches, perhaps at the end of the week or the end of the month. This creates a drag on cash flow. Invest in billing software (see below) to issue demands as soon as work is finished or goods have been shipped.

Automate where you can

Automation is the key to resolving these issues while saving you vast amounts of time and money. It removes the risk of human error while also freeing up your team to focus on other activities.

Electronic billing systems, such as Xero, QuickBooks or SAP, create a seamless end-to-end process with convenient features, such as the ability to track invoices, or allowing your clients to download your invoices directly into their own accounting system.

Most automated billing systems further break down the barriers to paying by allowing customers to click straight through via the invoice to settle their bill straightaway. This pay-now facility is proving increasingly popular as it boosts cash flow for the vendor and reduces accounts processing time for the busy customer.

Used alongside a cloud-based payments provider such as GoCardless, they can provide a fully-automated workflow complete with real-time notifications if anything goes wrong, such as a failed or cancelled payment.

Case Study

The benefits of automation are well illustrated by Propel by Deloitte accounting and advisory service, which recently automated its accounts receivable process using GoCardless.

The move allowed the firm to reduce its debtor list while also reclaiming at least two days each month that would otherwise have been spent on admin.

**Gemma Taylor, Propel's Technology Lead, says: "We had to spend time running and analysing reports to see if a client had paid us, as well as chasing those who hadn't.
We realised that we needed to automate this process.**

"Since moving to GoCardless, our debtor list has definitely decreased. If a payment fails or a mandate is cancelled, GoCardless automatically notifies us so we can follow up. Overall, it's really useful and a great addition to the apps we use to manage our clients."

Improve payment options

Another key part of optimising the accounts receivable process is to make payment as easy as possible for your clients. One way to do this is by offering clients a wider and better range of payment options.

Different payment methods come with their own pros and cons.

Cash and cheque

Traditional payment options like cash and cheques are still used, but they are slow, inflexible and inconvenient, especially for large firms handling substantial invoices.

Credit & debit cards

Cards are popular and convenient, but they risk churn when they are either rejected, expire, or get lost/stolen, with 5-15% of all card payments failing for one of these reasons.

They also attract high fees for your company.

Bank transfers

Collecting money by bank transfer is common too, allowing quick turnaround times, low fees and low failure rates, but the downside is their lack of flexibility and conTrol from the business collecting payment, plus the inability to receive notifications if a payment fails.

Direct Debit

To maximise flexibility and streamline your accounts receivable workflow, consider including Direct Debit among your available payment methods. →

With Direct Debit, companies can automate payments, taking money from clients' bank accounts whenever payments are due.

Payment frequency and amount can also be changed as required without having to seek client permission each time, thanks to the initial set up of a Direct Debit mandate.

Direct Debit is inexpensive and failure rates are very low (GoCardless clients typically enjoy failure rates at 0-2%, for example). It's a very flexible way to take payments, with minimal hassle involved, both for your finance team and for your clients.

Switching to Direct Debit can transform your cash flow management, cutting down uncertainty and risk by allowing you to predict when money will come in.

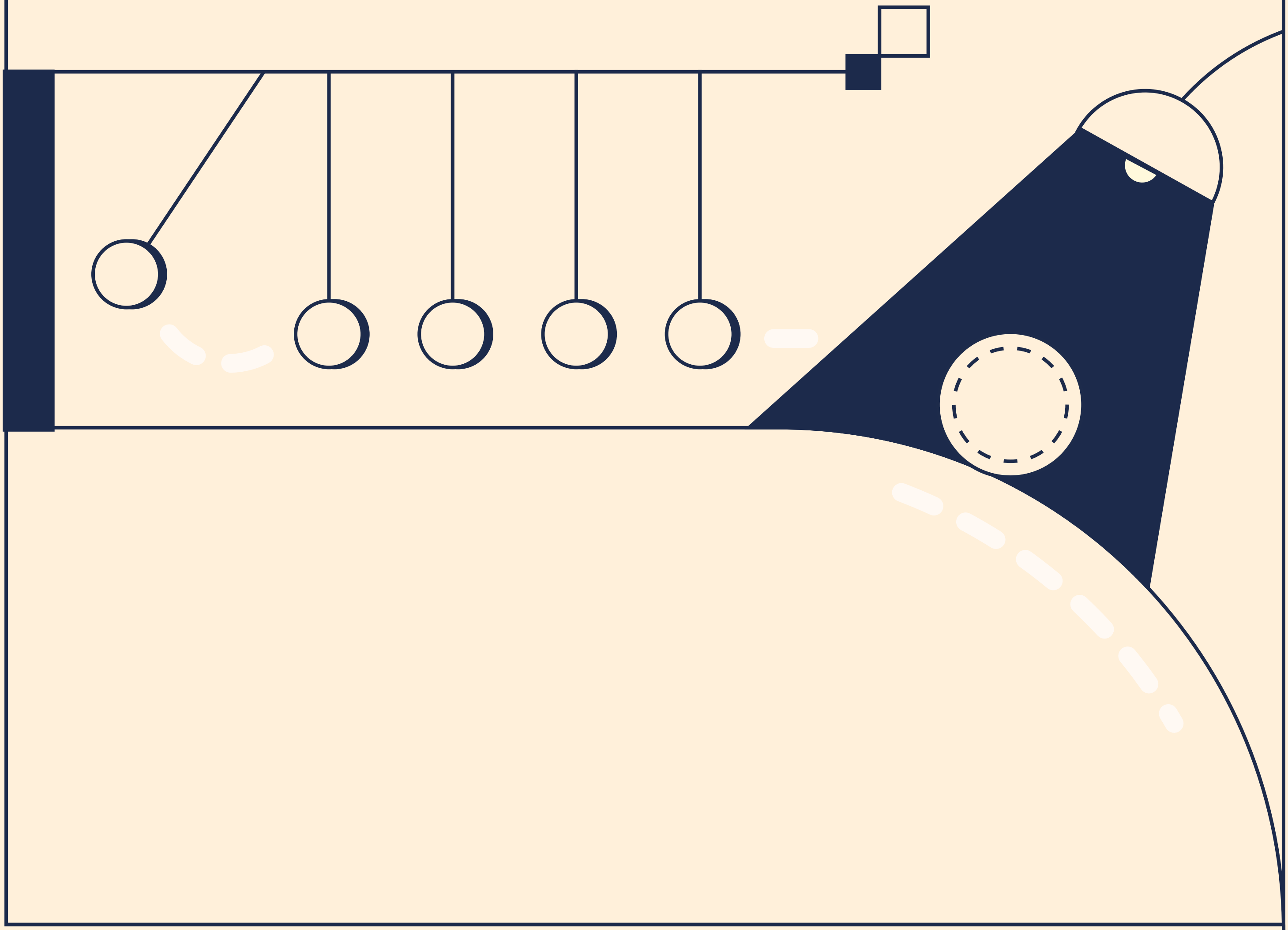
"Direct Debit is inexpensive and failure rates are very low"

Case Study

Unified communications company VIA was struggling with the heavy admin from payments made by bank transfer until it made the leap to Direct Debit. Now, 65% of VIA clients pay their invoices this way. What's more, VIA has now cut its debtor days by half.

"From a cash flow perspective it works perfectly," says Iain Worthington, Finance Director at VIA. "Instead of getting a dribble of funds, we get a significant proportion in one go. "Running any business is all about managing cash flow. GoCardless helps significantly, we can predict early on what we're getting in and manage outgoings accordingly."

Optimise your clients



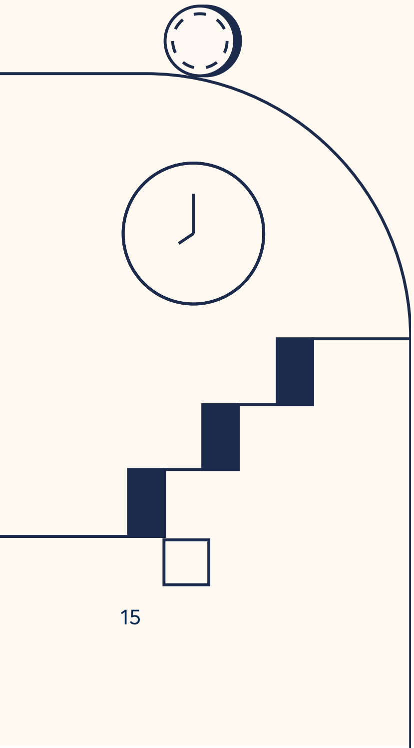
You've worked hard to make your accounts receivable process as efficient as possible, but the final piece of the puzzle is your clients. Taking extra steps to minimise late payments will complement your optimised internal processes while also further reducing cash flow risks. In this final section, we'll explore some ways to optimise your clients.

Send timely reminders

Much of the time, late-paying clients simply need a reminder. Your billing system can be set up to issue these by email at any desired length of time after the invoice date, or a few days before.

If reminders solve the problem then no further action is needed, and you've saved your team time and stress.

The tone of your reminders should become more urgent each time you are forced to send one to a single client.



Pick up the phone

Even in this age of automation, the human touch is still best for resolving tricky situations – such as clients who habitually pay late even after reminders. These clients may have genuine reasons for not settling their accounts on time. Picking up the phone early on gives you the option of working with the client to solve the issue, perhaps simply by changing the payment date or allowing them to pay in instalments.

"If your firm collects recurring payments from clients, you could minimise the risk of late payment"

It's not always easy to address late payment issues directly with clients, but, with some proper training, your finance team can soon become well-versed in addressing these issues firmly yet with sensitivity. What's more, if your firm collects recurring payments from clients, you could minimise the risk of late payments almost completely by encouraging them to pay by Direct Debit.

Charge interest to late payers

Many clients will respond positively when you reach out to them by phone. But despite the best efforts of your team, there will always be a few clients who continue to pay late, often without good explanation.

When this is the case, consider charging them interest on the outstanding invoice. Even if you later forgive it as a sign of goodwill, charging interest lets the client know that your firm is serious about collecting what it's owed.

You should make the interest charges clear in your internal policy, and also in the terms of the invoice itself. Doing so may help to address the late payment problem for future invoices.

Offer discounts to early payers

To encourage clients to pay early, you could consider offering discounts for early settlement.

For example, this could be a 2/10 net 30 arrangement, in which clients receive a 2% discount on an invoice paid in ten days, with the full amount due within 30 days if this early deadline isn't met.

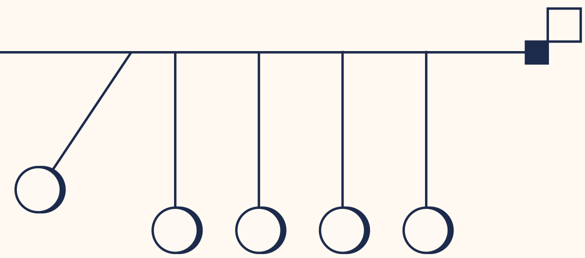
Some firms go even further and offer a 5% or 10% discount for a ten-day settlement period.

Cut off credit as a last resort

If none of the above methods work, then another option is to cut off the client's credit all together.

After all, by allowing generous payment terms on your invoices, you're effectively offering clients free financing – at your firm's risk.

To maintain relationships with your clients, be sure to clearly communicate that you're stopping credit as a last resort and that it can be rectified when you receive payment.



Conclusion

No matter how large or small your business, it doesn't make sense to let cash remain stuck on your balance sheet. Freeing up cash flow can benefit your business in so many ways – and this can be achieved largely by optimising your accounts receivable process.

We suggest using this two-step approach to this task, first tackling the internal process itself, and then improving your situation in relation to late-paying clients.

Automation certainly has a key role to play in making the process repeatable and scalable.

Improving your accounts receivable will always be a battle, and you can never rest when invoices are being sent to debtors all the time, but by combining the above tactics, you can reduce your debtor days as much as possible, making your cash flow much more predictable and sustainable.

Click here find out more about how GoCardless can help you get your invoices paid automatically, without the awkward conversations and endless admin.