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Streamlining the financial supply chain

How teamwork and technology can solve the problem of uncollected cash

According to research carried out by The Customer Value Group, the top 1000 in Europe are owed £185bn in uncollected revenue- a figure that equates to a quarter of all invoices in circulation at any one time.

The research also illustrates the dire culture of missed and late payments among UK companies and their customers: the 245 British companies contained in the sample are owed almost £40bn between them. As a consequence of this failure to collect, they lost an enormous combined profit opportunity of £1.8bn.

But what exactly is the problem? Are the debtors sitting on the invoices and purposely not paying them? Is bad practice on the parts of Accounts Receivables to blame? The answer predictably, is a combination of many things.

Payment Breakdowns

The breakdown of the research carried out by The Customer Value Group, which is a company spun-out of the respected benchmarking and consulting group Hackett-REL, offers an illuminating view of the financial supply chain. In the UK, almost £12bn of cash remained uncollected as a result of customers withholding payments because of ongoing disputes. £9.6bn was unpaid because of unresolved customer queries, while a massive £18bn came about due to poor collection practices.

According to the group's Managing Director Dickie Bielenberg, neither legacy systems nor traditional ERP or CRM platforms are designed to deal with how

poor customer service impacts on cash collections and ultimately, the bottom line. *'Our view is that legacy ERP systems are very functional, but they are not able to look at the reasons why customers don't pay on time...there's a huge disconnect,'* he said.

'The issues are huge. We have a company with a receivables balance of £280m, of which 50 per cent is overdue. If you improve the collection process you can radically improve cash flow'

In fact, it may seem flippant, but payment disputes often come about due to very simple reasons: customers may constantly be receiving goods late, they may have a notoriously bad credit history, and they may be dissatisfied with the goods or service received. The key challenge is working out what the issues are.

Control through technology

Technology has a hugely important role to play in an efficient Accounts Receivables department and the wider financial supply chain. Martin Williams, managing director of credit check company Graydon, explained that there are many ways that finance directors can look to improve efficiency – and although technology is just one of these, it is a hugely important one.

'There are all sorts of software packages that people can use to run the credit-management function, in terms of systems that drive actions (such as collection software and dispute resolution software)' he said. The likes of Microsoft, with its Microsoft Dynamics GP Financial Management and SAP with its Financials Accounting module, have developed technology to provide better views of cash flow and the real-time financial view of a business. And the Customer Value Group is forging a very successful business working out why clients don't pay on time and what needs to be done to counter this.

With the average company processing thousands upon thousands of invoices every single month, and the large multinationals processing millions, maintaining a tight control over the process is critical. While traditional ERP systems such as SAP are reasonably proficient at the billing process, beyond that they lack the intelligence to analyse what's really going on and why.

The close alignment of CRM systems and more intelligent analysis tools, allows companies to gain a far more holistic view of their credit function and what's really happening on the ground.

Do your research

However, Williams urges that this is still only part of the solution. Ensuring that a company's customers are willing and able to pay their bills before getting involved in a business relationship is another very important aspect of successful

credit management and, in this area, Williams claims that technology has come on in leaps and bounds over recent years.

Companies such as Graydon, Experian and Dunn & Bradstreet work with their client's 365-days a year. The entire ledgers of their clients are made available to credit-check companies, which are then cross-referenced against their own database and the results fed back to the client in question. As a result the clients get constantly updated feeds of information on the credit-worthiness of their customers. The data for the credit reports come from a variety of sources – from public references such as Companies House to payment data that is donated by third-party companies.

The lesson here is clear – companies are much more likely to have a positive financial supply chain experience if the companies they do business with themselves have a sound credit history, if they are traditionally good payers and if they are financially strong.

Getting paid

Another traditional bottleneck in the payment cycle is invoicing. How can companies guarantee that invoices are being issued when an order is placed, for example? One way is to implement electronic invoicing systems, a move that resulted in one company – M Barnwell Services, a manufacturer of sealant products with an annual turnover of £8.5m – improving cash flow by £200,000 and reducing debtor days by five.

'It's staggering how many organisations aren't doing it.' said Tony Bray, a director of VersionOne. 'If you look at medium-to-large businesses, it's probably around 20 per cent. But in smaller businesses, the figure is much higher than that.'

Traditionally, companies would print out all the purchase orders and stuff envelopes. Now they can just click a button and those purchase orders will be formatted automatically and intelligently, and sent out in the way the customer wants them (whether this be electronically, via fax or by post),' he said, 'If you can send documents electronically, typically it saves around £1 a document.'

Chasing debtors

And it's not just invoices that companies stand to save huge amounts of money from going digital with. By sending debtor letters electronically – something that may seem blindingly obvious to some – collecting overdue cash should, at least in theory and if the reasons for why the cash is late are understood, be made easier, quicker and cheaper.

However, technology can only solve part of the problem.

According to research carried out among the UK credit managers by the institute of Credit Management on behalf of *Financial Director* magazine, less than half said that they worked 'very closely' with their finance directors. Worryingly, almost a third said that they either did not work very closely with the same finance director or had nothing to do with him or her at all.

While it goes without saying that the finance director should not be getting involved in the nitty gritty of receivables and the chasing up of invoices, the old dictum continues to ring true: cash is king. A failure to maintain careful and strategic control over the credit function will result in a poorer cash flow and, ultimately, reduced profitability.

A core strategy

Happily, however, the research did pick up on some encouraging signs, with almost 90 per cent of respondents claiming that their companies did in fact see credit management as a strategic function to the business. Whether this was down to the fact the respondents were all credit managers with a higher opinion of their roles than is actually the case, or whether this is in fact the case, remains unclear.

But what is clear is that in order to improve the poor state of UK companies' financial supply chain and cash flow, finance directors must look at a variety of things: customer service and satisfaction levels, how closely the finance director works with the credit function and how credit worthy the business's customers actually are. And technology can help pull all of this together.

INTEREST CHARGES FOR LATE PAYMENT

What the legislation means

BusinessLink has published a guide to late payment legislation that outlines the updated *Late Payment of Commercial Debts Regulations 2002*. The regulations specify that a company should charge 8 per cent over the Bank of England's current base rate for a current six-month period following 31 December and 30 June.

So should, a company be owed £1,000 gross and it became late on 1 October, the rate would be 12.75 per cent simple (rather than the compound) because the debt became late during the six-month period when the Bank of England's rate was 4.75 per cent. This works out, if the debt has been outstanding for 30 days, to be 34.9p per day – or £1048 for the entire period.

More spectacularly, if you take into account the total value of unpaid invoices in the UK, according to The Customer Value Group, the daily interest charge under the regulations would reach more than £13.9m.