

WHITE PAPER BEST PRACTICES SERIES

ZERO SUM ACCOUNTS RECEIVABLE MANAGEMENT

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IMPROVE YOUR CASH FLOW
USING CASH GAP ANALYSIS

Zero-Sum Receivables Management Improve Your Cash Flow with “Cash Gap Analysis”

The “zero-sum” working capital tension between you and your customers requires strategy and a focused effort to enforce your invoice terms; you need to get your receivables paid on time. There are many companies that could improve their Days Sales Outstanding (DSO) by 10%, 20%, even 30%, if they use what we call Cash Gap Analysis to direct their efforts to the right customers at the right time, and employ technology to drive the collection workflow.

We recognize that a certain percentage of late payments are basically “baked in” to the system; that is, many customers have *no plans to pay to you on the date due*, and they never pay early. The best you can get is to get paid close to when the bill is due.

CREDITOR VS. DEBTOR IS A ZERO-SUM GAME

The best you can do is get your money and break even, and *still* they make you work for it.

- For a seller, the lower your Days Sales Outstanding (DSO), the better you are managing your working capital and accounts receivable.
- For a buyer, the higher your Days Payables Outstanding (DPO), the better you are managing your working capital, getting to what amounts to free loans from your suppliers.

To illustrate how passivity in credit and collection management can lead to worsening results, many Accounts Payable departments use software that tracks how quickly (or how slowly) you follow up for invoice payment, and then adjust the payment rules accordingly. *The less aggressively you follow up, the more slowly you get paid and vice versa.*

In addition, all manufacturers and distributors have hundreds of thousands and even many millions of dollars of cash “frozen” due to process errors, deductions, or disputes that are holding up invoice payment, yet few companies have invested in systems, staff or management to solve this. Once negative practices and habits become ingrained, they are hard to reverse.

How can you break this cycle and unlock this cash flow? Identifying internal and industry data that can solve revenue and profit dilution due to disputes and

deductions, and speed cash flow is no less important than optimizing your inventory management. Both assets depreciate, and both have the same impact on working capital. With bank lending constrained and always expensive, why not find growth financing internally?

Unfortunately, unless you have the technology and data to point you in the right direction, you're pretty much running in place instead of changing the course of events.

With fewer employees, the quality of data and collection systems have taken on critical importance for targeting collection, cash flow, and deduction management. What accounts receivable, collection and deduction management professionals know is that it is not merely how many you call (although that's important), but planning who you contact with what frequency.

Develop Your Scorecard to Identify the Cash Flow Gaps

1. Understanding where you are, relative to the best in your Industry, is the first step.
2. Use current industry and peer benchmarks to determine the improvement possibilities and identify what we call the cash flow "gap."
3. Compare your scores against the best performers in the industry, calculating the Cash Flow Gap in days and dollars on a customer-by-customer basis to give you a measurable target for your collectors. Set your DSO targets based on top industry performers, not the averages. Your best-in-class competitor's DSO could be 20 percent better than yours, indicating the improvement potential. Both on a general and customer-specific basis, you may find great opportunity.
4. Here are three hypothetical \$200 million companies, all in the same industry. We calculate the Cash Gap by comparing peer receivables data to determine the overall cash potential. General information, for public companies may be figured out from their 10Ks. However, aggregators of trade payment data by industry, such as Credit2b.com, are a more detailed and accurate source of this data.

COMPARE YOUR COMPANY PERFORMANCE VS COMPETITORS

Company DSO and Cash Gap For \$200M Revenues			
Competitor	DSO	Cash Tied Up In A/R	The Cash Gap
A (best)	37	20,276,000	0
B (average)	45	24,660,000	4,384,000
C (You?)	62	33,972,000	13,696,000

This analysis can be done for **each major customer** as well. You may be able get peer data from industry credit groups, or we can help you, as our Credit2B affiliate monitors trade payments from more than a million companies, including all of the retailers.

COMPARE HOW YOU ARE BEING PAID BY CUSTOMER VS COMPETITORS

Customer DSO Vs Industry Peers					
Customer	Peer 1	Peer 2	Peer 3	You (?)	Max DSO Gap
A	37	35	35	48	13
B	42	38	41	51	10
C	48	42	43	41	-1

Looking at a specific customer, you can determine the cash flow potential if you reach better DSO performance.

SEE HOW MUCH MONEY YOU ARE LEAVING ON THE TABLE BY CUSTOMER VS COMPETITORS

\$ 2,000,000 Customer Cash Flow Gap Vs Industry Peers							
Customer	Peer 1	Peer 2	Peer 3	You (?)	Max DSO Gap	Your Customer A/R Based on DSO	Cash Gap by customer
A	37	35	35	48	13	263,014	71,233
B	42	38	41	51	10	279,452	54,795
C	48	42	43	41	-1	224,658	-5,479

Your Cash Flow Improvement Plan

1. See how you compare with the best in your industry using [CRF](#) or [Credit2B](#) data in order to establish your performance goals.
2. Use an automated and collaborative collection and deduction management system that will prioritize action based on the risk, category, amount and age.
3. Track your cash flow results to make sure you are making the progress you anticipated and adjust if necessary.
4. Separate the deduction management function from collection management and have deductions handled by specialists who understand the complex business issues that create deductions.
5. Don't be afraid to escalate big problems. Have your president, for example, call his customer counterpart on a serious issue.

SUMMARY

Improving cash flow is a process, and it requires steadfast application of the best collection and accounts receivable practices. However, significant gains can be made which will improve your company's finances and provide working capital for growth. For more in-depth information on this subject, use the [Contact Us](#) page to request our in-depth [White Paper "Best Practices B2B Collection Strategies"](#).

About the authors: This paper was prepared by the Revenue Cycle Consultants at Smyyth/Creditek

Smyyth/Creditek provides world-class, end-to-end Order-to-Cash SaaS Technology (Carixa), and Outsourced Services, to enable companies to attain extraordinary cash flow and profits using best practices for management of credit, accounts receivable, collections, deductions, disputes and cash application.

The Carixa™ Order to Cash platform streamlines operations, slashes costs, and increases profits. Smyyth technology and services are built on Six Sigma principles and are Safe Harbor and SSAE16 compliant. www.smyyth.com

Carixa is a modular or an end-to-end solution for order-to-cash and is scalable from mid-market to the global enterprise. It comes with instant consolidation of subsidiary credit risks and receivables, collection and deduction management providing local operating power within a corporate policy framework. Need to centralize, decentralize, shift resources, or outsource? No problem, just set the policy and rules and it's done. Carixa integrates order-to-cash - credit, collections, deductions, reconciliation, EIPP, cash application, customer portals, and more.

For more information on Carixa or Smyyth services, we would be delighted to hear from you. info@smyyth.com www.smyyth.com