

## **Business Services - Common Problems:**

### **Decrease in collections from trade debtors**

As a percentage of working capital, the value of trade debts is too high. This means that the business's cash flow is restricted.

#### **Indicators**

- Decreasing cash or an increasing overdraft.
- Increasing value of debtors.
- Increasing average age of debts.

#### **Causes of the problem**

- Credit policy is inadequate.
- Debt collection program is inadequate.
- Debtors are failing to comply with specified payment periods.
- Customers are facing financial difficulties and so are reluctant to pay their debts.

#### **Short term solutions**

- Appoint an employee to contact all overdue debtors with a view to either receiving payment or gaining an adequate reason why credit terms should be renegotiated.
- Appoint a debt collection agency.
- Factor the debts.
- Ensure all customers are aware of the business's payment period and terms.
- Provide incentives for the early payment of debts (eg discounts for payments received within 14 days).
- If customers are in severe financial difficulties consider dealing with them on Cash on Delivery (COD) basis only.

#### **Long term solutions**

- Review the business's credit policy. If the business does not have a credit policy then one must be created. The credit policy should outline the amount of credit which is acceptable, the length of time for payment of credit which is acceptable and actions which should be taken to ensure prompt payment of debts. An important aspect of the credit policy is ensuring that customers are aware of the business's credit terms. If the business has a credit policy it should be reviewed to ensure it operates efficiently and is strictly enforced and that employees are fully aware of it.
- Set a desired percentage of working capital which trade debts should not exceed. Both an overall figure and a figure in relation to major individual debtors should be decided upon. The level of debt should be constantly monitored and if it reaches the set percentage early action can be initiated to avoid a financial problem being created.



- Establish a policy for 'target collections' each month and offer responsible employees incentives for reaching the monthly targets (eg free theatre tickets). The targets should be accompanied by guidelines for employee actions so that customers are not upset by over-zealous debt collection.
- Provide customers with incentives for early payment of debts or payment in cash. Incentives usually take the form of a discount.
- Move the responsibility for debt control to a higher level of staff/management to emphasise its importance to the business.

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