A/R > $:

Aging debt is just the beginning…

Introduction

Our beloved Finance professors taught us many lessons but none more powerful than TVM—time value of money. Cash in hand today is worth more than the same amount in the future. Our team at Catalyft has been fortunate enough to work with clients who have taken cash in hand to heart (or a bird in the hand if you're an aphoristic type…) and focused on empowering their teams to reduce aging receivables and accelerate cash flows without financial engineering (such as factoring). While the journey starts with the goal of reducing outstanding Receivables, teams soon realize they will need to alleviate customer and employee frustrations along the way to get those aging dollars back in the fold. When pursued with diligence and conviction, tackling aging A/R provides more than cash. These forthcoming words will touch upon several common cash constraint themes and foundational improvement lessons we have learned working with Accounts Receivable (A/R) teams on Order-to-Cash improvements over the years.

Let the data unearth the skeletons

When the Catalyft team first starts chipping away at the A/R mountain, most engagements began by simply—some may say naively—asking the Finance and Accounting team, "Why is this customer falling behind in payments?" No surprises here, we'd get the usual responses: "They always slow-pay us", "we're not a priority for them", "they're mad at us", "that's not my responsibility" - interspersed with a few refreshingly honest answers like, "That's a good question—I don't know".

All teams benefitted from a simple pareto analysis visualizing the reasons why customers are on the A/R list—always providing an eye-opening experience. One remarkable recent experience with a Business Services team showed about 40% of past due customers were attributed to the willful, slow-pay column, about 10% of the accounts were locked in some type of legal transition inhibiting timely payment (such as bankruptcy or company acquisition). However, the rest were late for more nuanced, less-readily-understood reasons. The data told us the other 50% of late-payers were struggling with constraints other than having a shaky wallet or a suspect definition of "on time".

Synopsis:
Understanding and controlling your Accounts Receivable processes, departmental roles, customer experiences, and technology usage will produce far more than aging dollars collected on time. A/R is a window into cash constraints slowing your Order-to-Cash cycle but also surfacing frustrations your customers and employees fight on a daily basis

Benefits:
Reduce employee and customer frustrations while freeing up cash to fund future growth

Sectors:
Based on Business Services and Financial Services engagements but applicable to any industry with fragmented client base, outdated A/R visibility, and disconnected roles and responsibilities

Financial Results:
10% to 22% improvement in cash acceleration

Favored Measurement Method:
Past Due to Total Billed baseline over 12 to 24 month baseline

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Making matters worse

Now, here's where the tale usually got interesting. Inevitably, there were several reasons why our clients found their customers' names on "The List" - some reasons can best be categorized as inherent problems within the customer's organization (changing A/P responsibilities, inability to get on wire transfers, Billy is on vacation that week, etc.). The surprises often arrived when clients saw how many self-inflicted wounds were being proliferated by their own team—having a hand in forcing customers to pay late. Most key employees were painfully aware broken processes, misunderstood responsibilities, and underleveraged technologies were causing problems— for customers and for their own teams. However, most teams were also so overwhelmed with their day-to-day responsibilities, they could not get out of their short-term myopia, coordinate the resources to understand the chain of issues, and invest the time to fix them. In some companies, the team slogged through using creative "work-arounds" - getting them moving but not building up any structural changes capable of alleviating frustration for their team or remaining useful beyond the employee's time in a particular role. A/R constraints tended to build up over time in environments struggling with role identities, improvement inertia, and a communal sense of being powerlessness to make a dent in the problem. It's not too much of a stretch to say most organizations we've collaborated with unwittingly created barriers for their customers to pay on time and stressed out their internal teams across departmental lines (including sales, operations, IT, accounting, billing, and collections) during their monthly battle. Now, let's touch upon a few commonly observed cash constraints causing repeated strife for both customers and team members.

Ah, yes, the skeletons…customer and employee frustrations

⇒ *Unhappy with Goods or Services:* bad news-your customer is not happy. Good news-your customer is conveying this by not paying as agreed. If our clients didn't know there was a service problem, late payments became the wake-up call teams needed to get on with uncomfortable but necessary conversations with customers, understand where products or services were missing the mark, and fixing the problem before their buyer's remorse ages as ungracefully as the Receivables.

⇒ *Abandoned or Ineffective Financial Disciplines:* at a point in time, most client companies had healthy processes and controls to keep A/R from unnaturally rising. However, the process was no longer working due to a bevy of reasons: employee turnover, training gaps, changing work priorities, misaligned compensation plans, obsolete tool sets, separate IT systems, unplanned changes overwhelming the process…(and the list goes on). Growing A/R should be the call to action that something is amiss and the organization needs to get back to winning ways of being in control.

⇒ *Billing Errors:* scrutiny of A/R patterns usually uncovered billing errors adding to the shared misery. Whether it was incorrect invoice information, wrong payment terms, or the means of invoice delivery being problematic, the billing process got in the way of a customer's ability to pay on time. Simple invoice audits uncovered constraints leading to aging A/R. Past examples of corrected billing constraints included payment terms not matching up with contract terms (ex. Invoice says Net 30 but contract says Net 45), outdated billing contacts, incorrect addresses (email and physical), and even unclear payment submission instructions.

Ah, yes, the skeletons…customer and employee frustrations *(continued)*

⇒ *Misapplied Cash:* Working on Order-to-Cash improvements allowed the teams to see process disconnects across departments. We've seen repeated challenges in applying payments to the correct accounts in a timely fashion. The customer thinks all is well because they sent their payment; however, the home team has yet to make the right journal entry to the correct account number. Companies may use multiple internal finance and billing systems to generate invoices for the same customer. Some firms had different process steps and workflow routing depending on the way customers paid the invoices. For instance, there was one team handling cash in lock boxes in one location that had nothing to do with ACH transfers, online payments, or checks received across multiple geographical locations. The more billing permutations within the company, the greater the chance of payments being hung up in internal process jumbles.

⇒ *Disconnected Internal Relationships:* Our Order-to-Cash engagements have been a powerful force to surface frayed internal relationships and mysterious roles and responsibilities. Yes, "Ice Cream Day" and "CEO Dunking Booth" also create some cross-departmental bonds and laughs, too, but these are fleeting compared to an Order-to-Cash overhaul. Most companies we've worked with assigned A/R management to folks in the Finance and Accounting teams. Some firms had a dedicated Collections team as a subset of Accounting; most of our clients asked their teams to wear multiple hats managing A/R along with budget developments, financial reporting, and ad hoc projects. While the Accounting teams knew the numbers and understood the current sense of urgency, it was usually the Sales or Operations teams who had the true relationships with the customer. Without clarifying who's contacting the customer, A/R activities could devolve into an ill-timed, confusing, and off-putting nightmare for customers. Making matters worse, most of the Sales and Operations folks freely admitted they would rather discuss anything but aging A/R with their customers. Lacking the relationship strength of their Sales and Operations colleagues, the Accounting teams did not consistently understand the context and business practices of the customers as closely as their Sales and Operations counterparts. There was also the on-going challenge of "I thought you were handling this". Most Sales and Operations teams saw A/R as an accounting function while the Finance and Accounting teams thought Sales and Operations should be actively involved with A/R management. To put a finer point on it, Sales and Operations tended to understand the customer more deeply, knew who to speak with, selected the most effective customer communication channels, and had a better sense of timing (when and where to broach an issue). Departments were not working together on A/R goals, acknowledging all the customer relationship hand-off's occurring, and seeing the repercussions of miscommunication when asymmetrical information remained welled up in particular departments.

⇒ *(Unfounded) Sense of Helplessness:* Our time working with Finance and Accounting teams has always been very rewarding collaboration experiences. The nature of these positions attract very analytical, data-savvy, well-structured, and reliable individuals. (Talk about great partners!) However, most teams we've worked with were also bogged down with an unhealthy predisposition—the teams thought they were powerless to make a difference in the realms of process optimization, service levels, and customer relationship management (in other words: expressing an external locus of control). They tended to take their positions to heart and only stay within the confines of their financial job descriptions. Finance and Accounting improvement teams should be tackling A/R and upstream Order-to-Cash functions —but they also have the data and organizational insights to help in redefining roles, influencing customer relationship management, aiding in data visualization, providing IT with their needs list, and sharing cash flow training with the rest of the organization.

Ah, yes, the skeletons...customer and employee frustrations *(continued)*

⇒ *Contract Compliance Woes:* Remember the aforementioned disconnect relating to payment terms on invoices versus contractual agreements? This example was relatively minor in impact and easy to fix compared with other issues uncovered on our Order-to-Cash optimization quests. Digging into Contract Compliance, Catalyft teams compared "what we said we would do" with "what we are actually doing". Working with compliance teams turned up all sorts of issues ranging from potential risks to the customer relationships to legitimate fees and revenue sources that should have been billed. Yet again, roles and responsibilities across departments tended to be obscure and there were disconnects—even hesitancies — in sharing information. For instance, Sales was aware of the potential for additional charges, Operations completed the work without the add-on charges in place, and Billing was not equipped with proper triggers to add legitimate but unseen charges to future invoices. Missing out on a stellar opportunity, most teams needed to build organizational awareness and a feedback loop of cash-constraining issues when drawing up future contracts. The more prescient teams learned from unprofitable mistakes and prohibitive contract language. They fed these pearls of wisdom back to Contracts and Sales - now wiser due to the contract having some miles on it.

⇒ *Challenging Data Aggregation and Visualization:* On the A/R side of the Order-to-Cash continuum, data played a crucial role in creating the call to action. Just seeing where to invest your time in cash collections activity helped to solve part of the problem. Some clients retained several finance and accounting software systems as they grew but had yet to consolidate the data flow, hence, no single A/R report to rally the team around and get to work. Other clients had data aggregated within one system but reporting was cumbersome to produce and even more perplexing to interpret. We've witnessed clients who reviewed A/R with reports so outdated and untrustworthy, they might as well have reviewed each and every customer status *line by line.* Without an easy-to-interpret A/R report, the teams were worn out with painful, time-consuming reviews. When teams could not easily see which customers would provide the largest cash infusion, they were overwhelmed, unfocused, and uncoordinated in their efforts. Most teams needed to be able to see A/R faster than they thought previously practical, accounts needed to be prioritized in a meaningful, highly visual way to ply their efforts in more lucrative actions, reporting access needed to be opened up for all team members contributing to A/R collections, and the reports needed to provide data for future Order-to-Cash improvements (such as A/R reason codes to watch moving constraints or "Coming Due" projections for "Past Due" clients).

⇒ *Collection Skills Gaps:* Whether the organization assigned part-time responsibility to A/R collection or employed a full-time team dedicated to nothing but following up with "Past Due" customers, most teams needed improved tools, better process understanding, and more meaningful skills training to get better at getting more aging balances off "The List" every month. We touched upon system access and reporting support earlier—all necessary but not sufficient to empower your A/R team. Stronger teams ensured their employees understood their role within the total customer relationship. Some Collections teams were isolated from the rest of Sales, Operations, IT, and the rest of Finance and Accounting. This type of set-up inhibited collaboration on a unified approach to engage and take care of customers in a consistent manner. Some Collections managers did not understand the difficulty inherent in asking people for money—or the fact that just making contact with the right person on the customer side was a puzzle in itself. Contact activity levels needed to match communication channels preferred by customers. Collections teams needed to have escalation points—right up to CEO and CFO—to ensure they had leverage in getting the invoices paid.

Ah, yes, the skeletons…customer and employee frustrations *(continued)*

Teams not considering their collections approach within the context of an integrated customer experience and pre-existing customer relationships struggled with increasingly aging dollars and higher employee turnover.

Making matters better

Depending on the complexity of the swamp you're draining, Order-to-Cash improvements can be months to years in the making — but cash acceleration can be sped up in weeks. Aging A/R is a great starting point because it lends itself well to prioritizing structural changes and process improvements upstream. While every organization has unique needs, our Catalyft collaboration experiences have taught us several avenues to improvement. Here's an overly simplistic A/R punch list culled from our time on Order-to-Cash wrestling teams.

Encourage and empower your team to:

1) **Understand the reasons behind past due balances beyond the usual assumptions and excuses for "why"?** Make sure your team can see the reasons behind the past constraints to A/R, current reasons popping up, and the common reason codes changing as they implement their attack plan to remove customer and employee frustrations. As Eli Goldratt impressed upon us, constraints will move. Previously insignificant reasons will become the future's dominating cash constraints. The team will have to tap them back down with customer-centric process optimization, new tools, and a healthy dose of cash flow vigilance.

2) **Prioritize impactable fixes - don't waste time worrying about what's out of your hands.** This may sound like we're advocating a firm grasp of the obvious. However, your team is bound to have differing perspectives on prioritization, a continuum of beliefs around one's ability to make an impact and control outcomes, and varying levels of patience. Some guidance: people tend to overestimate their capacity for change when thinking about a task in isolation of all the other "to do's" that must be done concurrently. Structure a prioritization workshop with multiple departments representing stakeholder interests, hash out the details, and emerge with one list of opportunities (include expected constraint removal value, necessary resources to stick with the prioritized list, preliminary task owners, and targeted timelines to implement agreed solutions).

3) **Do not leave cash flow responsibilities to a default, uncoordinated group of employees.** Define cash collection process inputs and outputs within the context of the customer's perspective. Get all necessary departments and expertise involved in A/R relationship management (Contracts, Sales, Operations, IT, Finance, and Accounting tend to be the collective keepers of the keys).

4) **Agree on a simple graphical representation of your A/R transformation engagement** (including baseline, cash target, and frequent actual performance updates) to see incremental results on your arduous journey. Most definitely, track all customer and employee frustrations your team is solving while herding the dollars. This list of wins will affirm you're quite serious about longer-term enterprise excellence rather than just making the quarter look prettier.

5) **Aggregate your data through your IT system or data mart to be able to see all A/R on a weekly basis as well as "Coming Due" balances for "Past Due" customers.** With the team now seeing both "Past Due" and "Coming Due", they will get in front of future dollars spilling over into "Past Due". Equally important, they will approach the customer and payment solutions in a more holistic, coordinated fashion rather than focusing just on oldest dollars, largest outstanding invoice, or the customer with the friendliest A/P department.

Making matters better *(continued)*

6) **Simplify your reporting structure - generate and distribute "The A/R Report" not multiple versions.** Make sure the report distribution list is updated regularly with an owner and a scalable maintenance process in place.

7) **Design dashboard reports with easy-to-read visuals and straight-forward calls to action** (this is an art just as much as a science). Make your dashboard the centerpiece of your review meetings. Most teams appreciate high-level visual summaries with drill-down capabilities across cascading data components. Work with the team to understand the lowest level of data they need to contact the customer; they must be well-prepared and ready to answer questions with facts.

8) **Speed up your reporting distribution** - weekly A/R reports work well because the team has time to see issues and correct them before customers wallow in the usual 30 - 60 - 90 day categorization purgatories. Word of warning: the team will groan at this frequency if they have gotten into the habit of looking at A/R on a monthly or, perish the thought, quarterly basis.

9) **Train your team to go about their daily | weekly | monthly collection activities with the customer experience in mind.** Share with your team customer service and experience metrics along with their cash-related contact activities. Design and support cash activities with the customer experience guiding team interactions, sitting next to your team in spirit during performance reviews, coloring future decisions, and maintaining an organizational presence-of-mind.

10) **Make sure every person on your team understands their respective role in generating future cash flows.** Educate your team on the power of controlling your firm's capitalization destiny by having multiple funding options for future growth. Do not assume this is just a Finance and Accounting responsibility or your smart, well-educated employee base understands their cash preservation and generation capabilities.

11) **Pay your folks for hitting cash targets.** If cash is important to your organization, then structure the compensation program to reflect this high organizational priority. Most companies we've worked with had bonuses based on revenue or cost savings goals but needed to add cash flow targets as well. Of course, the viability of a cash goal compensation plan will be contingent on an employee's role within the organization.

12) **Last, but not least, celebrate successes along the way.** Managing rising A/R balances and all the litany of reasons spurring lateness will take time. Your team will need and will earn a few pats on the back along the way. Set up correctly, progress will be seen *now* with clarity and certainty by all key cash influencers. (Thanks to your well-designed, simple visual from recommendation #4 defining where the team started, what's been achieved to date, and where the team is headed). By designing customer and employee needs into Order-to-Cash, progress will be accelerated well beyond cash flow statements.

If your Order-to-Cash push leaves the team with a new-found reverence for cash, a deeper understanding of their respective roles, an agreed process to thoughtfully coordinate multifunctional energies, and a way to ensure cash-constraining frustrations grow rarer by the day, then your A/R balances were worth far more than stated dollars.

Ready to tackle your own private collection of Order-to-Cash frustrations?

(We **love** this subject)

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