


Ebb & Flow

Follow these cash-management solutions to stay afloat





In 1999 when Mike Hickman became sole owner of East Ohio Machinery Co. (EOM) in Alliance, Ohio, he knew that the company was swimming in debt. Nevertheless, Hickman set to work, convinced that revenue from projects already under way would keep EOM running and eventually get its debt under control.

Unfortunately, that same year the unforeseen occurred: Several of his big clients filed for Chapter 11 bankruptcy, and EOM's cash flow slowed to a trickle. The company had no cash reserves, and its line of credit was already maxed out. Hickman resorted to putting up \$500,000 of his personal assets to sustain the business.

"I learned many things from that experience," Hickman reflects, "but probably most critical was the importance of knowing my company's cash standing at all times and what our short- and long-term obligations are. Now cash management is a regular part of our weekly staff meeting, and we always keep other company leaders informed about our cash position too."

Hickman and his team significantly improved EOM's collections by reducing the turnaround period for client invoice payments from as long as 90 to 100 days to less than 60 days. Collecting invoices quickly and employing conservative spending measures have helped the company stash earnings in cash reserve funds. "We're in a better place to weather the next slowdown or unexpected event whenever it arrives," Hickman says.

Save for the Slow Times

According to the Small Business Administration, more than 50% of small businesses fail within the first five years, with poor cash flow frequently cited as a top reason. But small business owners and cash-management experts say there are many disciplined practices that can help your company forge through seasonal slow-downs, unexpected crises or difficult market downturns.

Kristen Marie Schuerlein saw a shortfall in revenue for her Seattle-based marketing-strategy company in 2004 when she faced a personal health challenge. Fortunately she had followed some sound advice she once received from another small business owner: Devote 2% of your gross revenue to paying down debt, and sock away 1% in a rainy-day fund.

“That rainy-day fund, combined with our line of credit, helped our company stay afloat during our slow time,” Schuerlein recalls. Once her health crisis had passed, revenue shot up by 300% the following year. The resulting profits, in fact, enabled the entrepreneur to launch a second business, Affirmagy, which produces unique silk-screened blankets.

Make Smart Use of Credit

“I’ve seen few companies go out of business because sales go down,” says Jerry Mills, CEO of Phoenix-based B2B CFO, which provides chief financial officers for small and mid-size companies. “Most of the time they go out of business because they die the death of a thousand cuts.”

Mills, who recently published his second cash-management book, *Avoiding the Danger Zone: Business Illusions*, says one mistake that can lead to big problems is simply failing to maintain an adequate line of credit. “If you have sales of \$2 million, you need to figure out how much capital is required to support those sales



over a year,” Mills says. “You also have to get the highest amount possible on your line of credit when you don’t need it. If you go to the bank when you’re in a cash crunch, you’ll be less likely to get your line of credit increased.”

Another misstep for small businesses is to misuse their line of credit. For example, Mills advises against tapping into it to buy equipment. “If you use your line of credit to buy fixed assets, you may not have enough cash to pay for daily operating expenses,” he says. Instead he recommends securing a separate loan for equipment purchases to keep more of your line of credit available in case of a seasonal slowdown or an unexpected event.

Receiving the Receivables

Other smart cash flow practices go beyond maintaining a healthy line of credit and using it effectively. According to Julie Lenzer Kirk, who works as a small business consultant and teaches entrepreneurship at the University of Maryland, Baltimore County,

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an area that small business owners too often neglect is one that should be among the most obvious: collections. “Some entrepreneurs don’t understand the difference between income and cash flow,” says Kirk, who previously ran a software company in Maryland for 10 years. “You can have many customers and still go broke if you’re not collecting your invoices in a timely manner. It happens all the time because entrepreneurs get too busy, and by neglecting accounts receivable, they unintentionally run their businesses into the ground.”

Collecting cash quickly may be a challenge if you’re dealing with big companies that often take 60 to 120 days to pay, Kirk concedes. When she ran her software company, she addressed this problem simply by charging interest to slow-paying clients. “The companies understood it was just business, because they wouldn’t hesitate to charge interest to their own slow-paying customers,” she explains.

To shorten the amount of time it takes to collect payments from smaller clients and individuals, some business owners take a different tack: They offer incentives that encourage clients to pay bills quickly. Chris Roush, who heads the accounting services team at Rea and Associates, in Millersburg, Ohio, specializes in serving small businesses. He advises certain clients to offer a 2% discount on invoices paid within 10 days. He also suggests following up on accounts receivable before they become past due. “The squeaky wheel gets the grease,” he says.

Schuerlein, who also suggests offering a discount to clients who pay invoices early, urges business owners to take one further simple step: enclosing a self-addressed, stamped envelope with every bill. “I’ve found that when you make it easier for your clients to do business with you,” she says, “your company’s invoice rises faster to the top of the payables pile.”

Sometimes, of course, you are on the other side of the equation with a need to reduce—or put off—your accounts payable. Kirk reminds her clients that they have the power to renegotiate terms of payment with suppliers and vendors. “Just because you have an agreement that says you must pay within 30 days doesn’t mean you can’t renegotiate those terms, especially when times are slow,” she says. “I’ve found that even lawyers and accountants are willing to put you on a payment plan, interest-free, because they value you as a long-term client.”

Finally, Mills advises, don’t make cash management a complex issue: “It all comes down to doing some planning, spending your money wisely and getting professional help when cash control becomes overwhelming.” ■

Turn Tax Into Cash

When evaluating your company’s cash flow practices, make the most of smart tax strategies

Chris Roush, who heads accounting services at Rea and Associates, reminds his clients that reducing tax liability can also help them control cash for their businesses. For example, when companies expect revenue to decline, they should lower their estimated quarterly federal and state income tax payments to keep more

money in their coffers for when they need it most.

Roush also finds that many small businesses overlook the research-and-development tax credit. Companies can take the credit regardless of what profit they made from the product developed, even if it tanked in the marketplace, he says.

Finally, Roush tells his small business clients that Section 179 of the Internal Revenue Code allows them to deduct the total cost of equipment the year they buy it, rather than depreciate it over several years.

For any tax-related questions, always consult a tax professional.