Cash flow is the lifeblood of any organisation. Companies in the private sector generally focus on increasing profits, but it is inadequate cash flows that can cause serious financial difficulties.

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CIPS Australasia - Cash Flow and Payment Terms

With increased fuel and food prices and predictions of a US recession, never has there been a more important time to track cash flow. As value protectors and risk managers, this is a key role for the procurement function.

Cash flow is a major concern to SMEs and often threatens commercial survival. Several large retailers in the UK have recently raised their payment terms to 75 days from the end of the month of invoice, with a further percentage discount for paying within these terms. The impact of this on the rest of the supply chain could be any of the following:

- Vulnerable suppliers in your supply chain;
- Suppliers covering the cost of late payments into their products or services;
- Supplier providing a lesser standard or quality of product or service due to having to cut costs;
- Inflating prices in the supply chain and/or market;
- Becoming unattractive to suppliers and having fewer responses to tenders or future work;
- Can create poor buyer-supplier relationships.

Supply Management last month reported that “A study of 1,500 small companies by the Forum of Private Business (FPB) found 88 per cent were not paid on time by their larger customers. The majority of the respondents, 72 per cent, said their standard billing period is 30 days - the legal maximum before a payment is classified as "late".

Some 56 per cent said late payment had become worse over the past year. Just under a third were owed between AUS$2,150 and $10,787.

Nick Palin, finance and administration director at the FPB, said in a statement: "Supplier abuse appears to be widespread and many smaller firms are in a catch-22 situation, fearing that if they take action and use the legislation to charge interest, these larger companies will simply refuse to deal with them again.

“Nearly all of the small firms questioned called on the government to do more to tackle the problem of late payment. In addition, 72 per cent of the vendors suggested the credit crunch is having a serious impact on their businesses.”

Legislation

The Late Payment of Commercial Debts (Interest) Bill 2003 was introduced to provide for interest to be levied on the late payment of commercial debts in relation to the supply of goods and services. This piece of legislation is particularly important for smaller organisations that have cash flow concerns as they are able to apply interest charged to any late invoices. It is always advisable to avoid any legal course of action if possible and always try to resolve or come to an agreement through the usual relationship management procedures. Further information can be found on the following link:


What can the P&SM professional do?

- Firstly, recognise that your supplier has the right to seek legal redress for payment made late according to contract terms. Payment obligations should be built into the company Corporate Social Responsibility (CSR) effort (Business Standards). Paying bills on time is part of being a good corporate citizen.
CIPS Australasia - Cash Flow and Payment Terms

- Make payment issues an integral part of your supply chain. This starts with credit checking potential suppliers (part of pre-contract supplier evaluation) through to invoice reconcili-
ation. Organisations should have a standard referral/approval process in the event of an in-
voice error or dispute.
- Seek to achieve fair and equitable payment terms with your suppliers and incorporate them into your terms and conditions of contract. For example, electronic invoicing
- (eInvoice), also referred to as ‘Electronic Invoice Presentment and Payment (EIPP) may be beneficial to both you and your supplier. Automated web-based purchase-to-pay (P2P) sys-
tems may be used where appropriate, to facilitate the payment process and eliminate the need for manual intervention. More information can be found on the eBusiness section of the Professional Resources area of the CIPS website (www.cips.org).
- Pay your invoices on time (according to contract);
- Monitor, measure and report on the effectiveness of your payment systems, setting inter-
nal service level agreements (SLA’s) for procurement and finance;
- Gain senior management commitment for a process to clear disputes quickly;
- Communicate your company payment policy with your Finance Department. The procure-
ment professional may be able to factor in a genuine discount from the supplier for earlier payment;
- Consider the rules relating to operating in territories outside your state and/or country, and any special considerations for foreign currency transactions/payments;

Summary

CIPS recognises the importance of cash flow to organisations working within the global economy. As well as being a strategic business issue, the procurement professional needs to recognise the statutory responsibilities afforded by late payment legislation.

Buyers must set a responsible set of payment terms for their supply base that allows as much competition as possible, whilst ensuring that you have a robust, sustainable and secure supply base.