Manage your Cash Flow Better by Rethinking your Accounts Receivable Ageing

Most of us are familiar with the traditional **accounts receivable (A/R) ageing report.** First, each customer's account is analysed to determine the age of each outstanding invoice. Typically, the time demarcations are **"current, 30, 60 and 90+ days."** Then, all of the customers' breakdowns are summed by ageing period. The traditional ageing report then shows each ageing period's total as a percentage of total A/R.

In fact, **this traditional report masks your actual collection success, particularly if your monthly sales vary significantly.** The new receivables resulting from large sales in the current month can cause smaller proportions to show for the ageing periods in arrears. You would deduce that your old A/R collection is under control, since the proportions fell from prior period comparisons.

New Approach to Accounts Receivable Ageing

To better assess the collections process, let's look at receivables in a different way. Instead of comparing outstanding balances by time period, we'll compare the amount of receivables uncollected as a percentage of the sales from which they were generated. **"new-look ageing"** uses the same raw data as before, but also requires the monthly amounts of credit sales.

The new-look ageing report shows the current, 30 day and 60 day receivables totals as a percentage of the relevant credit sales in the month they arose. Thus, in December, for instance, the current A/R arises from December credit sales, while the 30 day A/R arises from November sales and the 60 day A/R arises from October sales. (Note that this approach doesn't work for 90+ days A/R since they are derived from multiple previous months' sales.)

Compare the traditional ageing report on the left for the months of November and December, and note that December was a seasonally high sales month. A review of the summary totals shows that the current and 30 day statistics are consistent between the two months and the 60 day category improved. Good job, collections!

Now compare our new-look ageing report on the right for the same two months. The speed of collection of current month sales was consistent in November and December. However, our collection of prior months' sales slowed down in December (60% vs. 47% uncollected). Meanwhile the second prior month improved slightly.

Benefits of 'New-Look Ageing' Approach

The value of new-look ageing analysis is not so much in comparing two months, but in other comparisons. To do this, the new-look monthly current-30-60 statistics should be transferred to an excel sheet – which collects this raw information longitudinally across time. We'll call this the input sheet. As many years of data accumulate, the input sheet can be linked to other worksheets in the same file to give us multiple looks at the collection process. Each of these worksheets can present a sliced-and-diced analysis in both tabular and graphic format.

Traditional A/R Ageing Process

Ageing Report - November		Nov	Oct	Sep	Aug
Receivables Outstanding					
Customer ID#	Total	Current	30 days	60 days	90+ days
18	$ 16,100	$ 12,000	$ 3,300	$ 800	$ -
256	9,350	8,000	1,350	-	-
27	11,800	7,000	3,500	1,300	-
48	15,400	9,200	4,000	2,200	-
52	12,600	8,500	3,200	900	-
94	15,100	11,000	3,500	600	-
	$ 80,350	$ 55,700	$ 18,850	$ 5,800	$ -
Percentage of Total A/R		69%	23%	7%	0%

Ageing Report - December		Dec	Nov	Oct	Sep
Receivables Outstanding					
Customer ID#	Total	Current	30 days	60 days	90+ days
18	$ 31,600	$ 22,000	$ 7,000	$ 2,000	$ 600
256	7,500	5,000	2,500	-	-
27	23,900	18,000	5,000	900	-
48	21,600	15,000	5,000	1,100	500
52	34,450	26,000	7,400	850	200
94	29,900	20,000	9,200	700	-
	$148,950	$106,000	$ 36,100	$ 5,550	$ 1,300
Percentage of Total A/R		71%	24%	4%	1%

New-Look Ageing Approach to A/R Ageing

Ageing Report - November		Nov	Oct	Sep	Aug
Credit Sales in Month		$ 60,000	$ 40,000	$ 35,000	$ 50,000
Receivables Outstanding					
Customer ID#	Total	Current	30 days	60 days	90+ days
18	$ 16,100	$ 12,000	$ 3,300	$ 800	$ -
256	9,350	8,000	1,350	-	-
27	11,800	7,000	3,500	1,300	-
48	15,400	9,200	4,000	2,200	-
52	12,600	8,500	3,200	900	-
94	15,100	11,000	3,500	600	-
	$ 80,350	$ 55,700	$ 18,850	$ 5,800	$ -
Percentage of Relevant Sales		93%	47%	17%	N/A

Ageing Report - December		Dec	Nov	Oct	Sep
Credit Sales in Month		$115,000	$ 60,000	$ 40,000	$ 35,000
Receivables Outstanding					
Customer ID#	Total	Current	30 days	60 days	90+ days
18	$ 31,600	$ 22,000	$ 7,000	$ 2,000	$ 600
256	7,500	5,000	2,500	-	-
27	23,900	18,000	5,000	900	-
48	21,600	15,000	5,000	1,100	500
52	34,450	26,000	7,400	850	200
94	29,900	20,000	9,200	700	-
	$148,950	$106,000	$ 36,100	$ 5,550	$ 1,300
Percentage of Relevant Sales		92%	66%	14%	N/A

Process

By Roy Quinones, CMA and Don Nilson, CMA, FCMA

For starters, the input sheet might simply graph the current/30 day/60 day statistics longitudinally across many years. Management's review of this look may give a leading indicator of troubled times around the corner, as the velocity of money slows down and customer tardiness increases.

Another worksheet might draw from the input sheet to compare in tabular form across the years each of the current, 30 day and 60 day statistics month-to-month. This data can be depicted in a series of three graphs as well (one each for current/30 day/60 day statistics), showing the twelve months of the year on the x axis and the percent uncollected on the y axis (see Historical seasonal comparisons 30 day graph). This look might indicate seasonal comparisons. If there has been employee turnover in the collections department, this information might provide some early feedback on the success of the current staff.

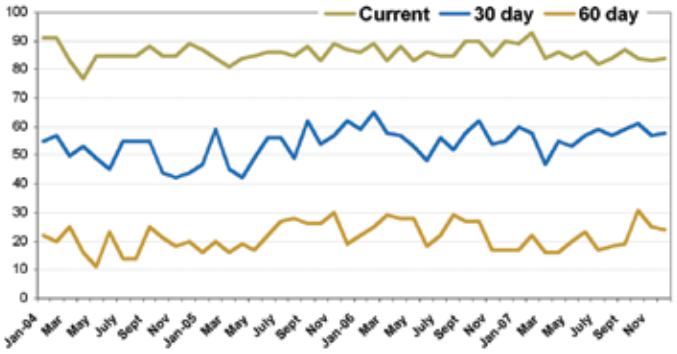
Another worksheet look might focus on the collection trend over the current/30 day/60 day evolution. Our success at collecting, for instance, January's credit sales is tracked by the current statistic in January plus the 30 day statistic in February and the 60 day statistic in March. This worksheet would draw its data from the input sheet as well. Twelve graphs could be created for each month and the current/30 day/60 day statistics can be visually compared (see the January sales collection graph). Management's review of this look may identify and normalize monthly experience across time or, on the contrary, flag attention to problems or successes.

In the case of the long term trend graph, excel can easily be used to produce regression trend lines to provide further insight.

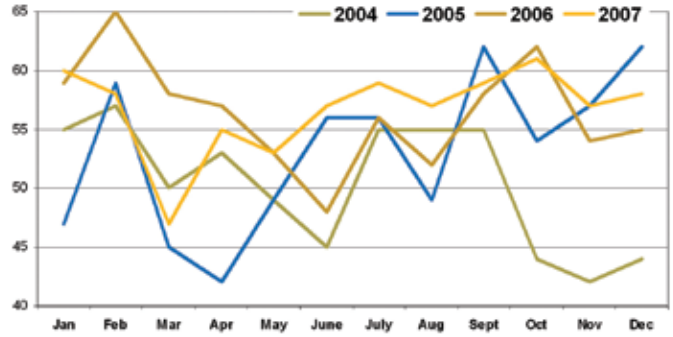
Management can precipitate the value of the new-look ageing approach by having a staff member dig out the necessary historical data to create the input worksheet.

We think that new-look ageing gives a fresh and valuable input to the critically important collections process. As the economy turns down for a while, the old saying "cash is king" is even more important.

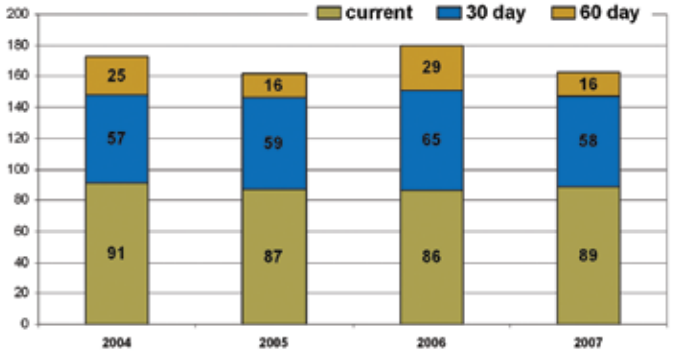
Long term trends



Historical seasonal comparisons 30 day



January sales collection



Roy Quinones, CMA *is a Financial Analyst with Powerex. Roy is also a member of the Update Editorial Task Force.*

Don Nilson, CMA, FCMA *is the Principal at Nilson & Company. He is also a member of the Update Editorial Task Force.*