



Managing your suppliers of finance

The most obvious supplier of finance to your business will be your bank but there are probably a number of others you haven't considered. Managing the businesses relationships with all of your suppliers of credit has never been more important.

Here are practical ways of keeping the suppliers of finance to your business inside.

Who are they?

Finance is elemental; no business can survive without it. You may think that it is only your bank who supply credit to your business. You will probably get credit from your suppliers for your materials, overheads and stock. Your fixed assets may be financed by hire purchase or lease agreements, you may have non-bank loans from say the Carbon Trust or family members, you may owe money to the financial institution which provides you with invoice discounting, you may have local authority grants, you probably owe money to HMRC, you may have a director's loan account and you probably have shareholders. Some of your customers may pay you in advance so you owe money to them too!

Let's look at some of the key suppliers of credit to most businesses and see how we can ensure that we create and maintain healthy business relationships with them and use them to best effect.

Credit rating agencies

Although credit rating agencies are not a source of credit, they do influence the amount of credit which your suppliers will be willing to give you. Most businesses now have credit approval procedures and given the low-cost and ready availability of credit rating agency reports they are used widely.

Two factors have resulted in a deterioration in the credit rating given to many businesses. Firstly, as a result of the recession, the major credit rating agencies have changed their risk assessments of certain industry sectors. So even if your financial results are holding up your credit rating may be weaker. Secondly, for the businesses who have filed their 2009 financial statements, and where these figures are poorer than 2008, the decline in performance is reflected in a weaker credit rating.

You should establish your credit rating with the main agencies (Dun & Bradstreet, Equifax, etc). Speak to the agency to confirm that they have classified your business in the correct sector; this can make a big difference. And, ensure that they understand your balance sheet. When preparing your annual financial statements, discuss the classification of liabilities with your accountants. The greater the proportion of liabilities which can be classed as "due after more than one year" rather than "due within one year" the stronger your credit rating.

Trade creditors

As well as supplying you goods and services, your suppliers also supply you with credit. The more credit you can get from your suppliers the less credit you have to get from other sources. Trade credit is an excellent source of finance to your business. It is generally free and unsecured. It is better to owe £100,000 to your suppliers than to your bank – no interest charges, no arrangement fees and no security. If you are on good terms with your suppliers consider asking them for extended terms - it is about as close as you can get to a free lunch!

We all like to be paid on time. If you can pay your suppliers on time then do so. If you can't, contact them and agree revised payment terms. I know it may sound like a cliché but timely and honest communication is essential to creating and maintaining good relationships with your suppliers. If you demonstrate to your creditors that you are on top of the situation, even if you are behind with payments, they will have more confidence in you and will be more likely to cooperate with you.

Avoid making lump sum payments; this is seen as a warning sign that you are struggling. It is always better to pay specific invoices.

Banks

I have seen instances where the fact the bank has felt it has been misled by a business has been a key factor in them deciding not to continue supporting a business. I make no apology for saying again – timely and honest communication is essential.

If your business has significant bank debt then they have probably asked you for regular financial information. The bank may also have advanced the funds to you on the condition that your business maintains certain financial ratios. These types of requirements are referred to as covenants. If you breach your covenants the bank may have the right to withdraw the funding or renegotiate the terms. Unless you've been on the moon for the past 18 months you'll be aware that banks are using every opportunity to re-price facilities and switch pricing from base rate to LIBOR – in the words of the song "the only way is up". Keeping on the right side of your covenants is crucially important.

If you don't know what covenants you signed up for – find out; check the facility letter your bank sent you when you initially drew down the finance.

HMRC

You may think that this is an unlikely source of credit. The Business Payment Support Service is designed to help companies and the self-employed who are not able to pay their taxes on time. It covers, corporation tax, income tax, VAT, PAYE and National Insurance. In most cases you can make an agreement over the telephone to settle tax liabilities by instalments.

This source of credit has been a lifeline to many businesses.

Moreover, if you owe corporation tax or income for last year and expect to make a loss in the current year, HMRC will now take the anticipated loss into consideration when rescheduling the payment of the previous year's liability. In effect, you are getting loss relief up front.

You

It is common for directors of private companies to give a loan to their company. The amounts involved can be substantial. It is rare for this type of loan to have any documentation; an omission which could leave the director exposed.

The existence of loans from directors is often a symptom of funding difficulties. If you are owed money from your company consider the company making loan repayments to you rather than salary payments. As the loan repayments are free of NIC and PAYE, you can get the same cash in your hand every month for a much lower cash outflow from the company.

Shareholders

I've seen a number of companies who have moved from the start-up stage to having 3rd party shareholders make mistakes with their shareholder relations. Whilst the entrepreneur recognises that the new shareholders have provided funds, he or she fails to see the need to keep the shareholders up to date. This is not a good start to the relationship.

There are lots of things which from a legal perspective you may not need to tell your shareholders about, but if you want them to support you and provide further rounds of funding you ignore them at your peril. Agree the frequency and format of reporting to shareholders and stick to it. ■