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Six money-management mistakes and how to fix them

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As Eric Lange and other Canadian entrepreneurs know, little matters more to a business than maintaining a healthy cash flow.

Mr. Lange, for one, says diligent cash-flow management and planning has helped keep his family-run business profitable every year since it opened in 1986. Lange Transportation and Storage Ltd., with an office and warehouse in Mississauga, Ont., and another warehouse in Edmonton, has 40 full-time employees and brings in $6-million to $10-million annually.

Mr. Lange, whose other ventures include the hobby business Toronto Maple Leaf Licences, says his accountant projects the cash generated and available, as well as the expenses, on a weekly and monthly basis.

"As we go through the year and see unexpected expenses, we try to adjust the expenses we have control over," Mr. Lange adds. He also takes advantage of credit card reward programs to save about $30,000 a year in travel expenses, and has worked out deals with many of his clients to have them prepay for services, to ensure cash flows into the business as quickly as possible.

According to chartered accountant Frank Fazzari and other experts, keeping on top of cash entering and leaving a business, as Mr. Lange and his accountant do, is the most basic yet crucial aspect of cash-flow success, but it's sometimes overlooked.

"It is somewhat shocking when an owner wants for us at the end of the year to tell them whether they are making money," says Mr. Fazzari of Fazzari and Partners LLP in Woodbridge, Ont. "If they wait until the end of the year, then there are likely problems that could have been avoided."

Nancy Harris, general manager and a vice-president for Sage Simply Accounting based in Richmond, B.C., says smaller establishments can be especially at risk of a cash crunch.

In fact, a 2011 Angus Reid survey conducted for accounting software producer Sage found 26 per cent of the 503 small business owners surveyed cited managing their finances, including their cash flow, to be the weakest area of their businesses, second only to dealing with taxes at 47 per cent.

"Smaller businesses are more commonly stretched thin, and it may take a while for a lot of them to determine what their best practices are," Ms. Harris says. She adds that "proactive planning" helps in creating a "formula" for knowing how much cash you should have on hand, based on the ebbs and flows of a business.

John Harris, of the Vancouver accounting and business advisory firm Grant Thornton LLP, stresses that "whether a company is profitable or realizes losses, liquidity is important … to maintain the day-to-day operations."

Adds David Wilton, director of small business for Bank of Nova Scotia in Toronto: "Cash is the lifeblood of a business – any business can survive a downturn in sales, but can't survive not having any cash, so make sure cash flow is predictable and that you avoid some things that can create a crisis."

Here are six common cash-flow errors and how to avoid or fix them, according to experts:

Error: Not having a reliable cash-flow planning and tracking system.

Fix: Use special accounting software and online interactive tools that can help in cash-flow tracking and forecasting (i.e., what is likely to happen to a business over a day, month or year). For receivables, for instance, programs and online tools can send electronic invoices to clients with a link to a portal where bills can be paid online. Mr. Fazzari says a company's accountant "should be providing the owner with information regularly. … No information means no cash-flow management."

Error: Mismanaging or avoiding credit.

Fix: Prearrange credit (such as credit lines or cards) through financial institutions before you need it. "You want to be proactive – if your cash flow is tight and you're experiencing challenges, it will be more difficult for you to go to a bank and get it," says Mr. Harris. If using credit to defer cash outflow, ensure it's paid back before high interest rates kick in, Mr. Fazzari warns.

Error: Waiting too long to collect from customers.

Fix: Negotiate prepayment plans with customers, or encourage them to use credit or debit cards. The goal is to avoid letting receivables (what customers owe you) get out of step with payables (what you owe). Also, don't allow receivables to get too old, and risk going to collections. "Anything you can do to speed up receivables will help with cash flow," Mr. Wilton says. Mr. Harris of Grant Thornton warns that before accepting credit cards from customers, check out their credit backgrounds.

Error: Neglecting your bills and taxes.

Fix: Pay tax, supplier and other bills on time to avoid high penalties and a bad credit reputation. Know when your bills are due (use programs or online tools to alert you about bill due dates and set up pending payments), and pay them as late as possible without incurring penalties. Mr. Harris of Grant Thornton encourages taking advantage of any early-payment discounts, if they're worth your while. If you can't make a payment on time, "have that conversation with vendors and let them know your situation," says Ms. Harris. "You may be able to negotiate a payment plan."

Error: Not planning for growth.

Fix: If your company is experiencing significant sales or expansion, update your cash-flow plan and projections to take the implications of growth into account. "Businesses find cash flow comes under the biggest demand in rapid growth situations, which means you have to start funding more inventory, more receivables, higher expense levels," notes Mr. Wilton. Experts say rapidly growing businesses can also benefit from hiring a special adviser, such as a chartered accountant, to aid in growth planning.

Error: Not paying yourself.

Fix: Include a reasonable living wage for yourself in business and cash-flow planning. "We often hear, 'Well, a business likely won't make money in the first two years,' but if can't pay yourself for two years, you won't be able to build your business, so you have to build in a personal wage," Mr. Wilton says. "If you go into a personal cash-flow crisis and need to pull cash out of the business, you've also created a business cash-flow crisis."