

Partner's Report for CPA Firm Owners

September 2006

INCREASING MARGINS: Boost Revenues for the Year by Honing Collections Practices Now

Do you know your firm's average time for collections? This is a benchmark that every owner should be familiar with. If it is over 60 days, you and your fellow owners ought to be working to cut this time.

Why is now the time to do this? Because the fall is most likely your second busiest time of the year—and the last big push toward maximum revenues for the year, if you are on a calendar-year schedule. Even if your fiscal year ends at another time, getting your collections practices in order now will help your firm bring in revenues and maximize cash flow in plenty of time for the 2007 busy season.

A delicate balance. CPA firm owners are often reluctant to insist when it comes to collecting payments. Owners fear that doing so will damage their relationship with clients. As a result, most firms simply rebill and follow up with telephone calls encouraging at least partial payment if a client is in financial distress.

When is it time to turn to a collection agency? Most owners would say this is a last resort. *PR* says it depends on the client, its history of payment with the firm, the size of the engagement bills, and a number of other issues. For clients who are repeat offenders—especially those that present other problems—you may not be interested in continuing the relationship anyway. The most difficult scenario is when you want to keep the client, but also need to be paid for your firm's work.

Hiring professionals to step in and help may be the best way to get your money, since the likelihood of collecting on these outstanding receivables decreases substantially over time (see the accompanying figure—based on data from the Commercial Law League of America and the International Association of Commercial Collectors—which breaks down the effects of longevity on the collectability of an invoice).

If you feel as though your firm is the only one using a collection agency, be assured that this is not so. Third-party collection agencies—historically focused on consumer debt—are continuing their steady expansion into the commercial-debt arena, according to the U.S. Census Bureau's most recent Economic Census report. Since the recently-released report is based on 2002 data, there is every reason to assume the statistics significantly understate the current role of third-party collection agencies in commercial collections.

The Economic Census report reveals that fees earned through commercial collection activity in 2002 represented 28.7% of total industry receipts—up from 21.9% in 1997. Over the same period, consumer collection activity declined from 73.7% to 67.6%.

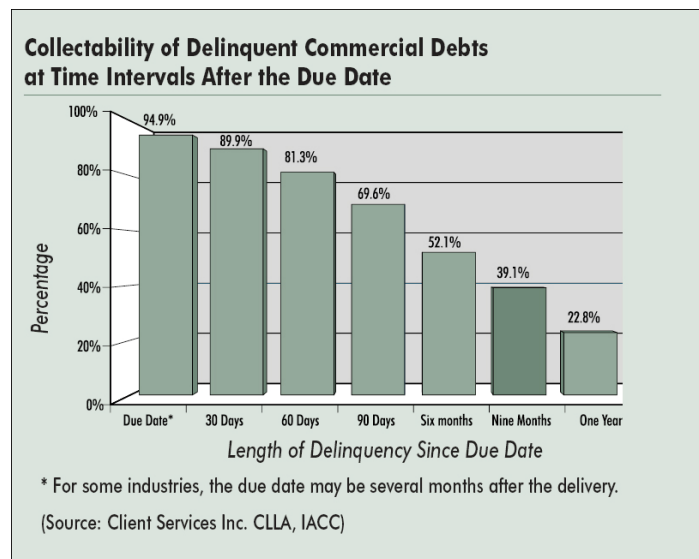
Choosing your collection agency. If your CPA firm is at the point where an outside collection agency is the only option, you'll need some guidance on how to select the best one. *Why?* In addition to the sheer number of third-party collection agencies (see the accompanying sidebar), there are many variables involved in choosing such a partner.

The guidelines presented here aim to both help you select the agency that will get you the best results *and* to maintain a successful, ongoing relationship with the client (if your firm chooses to do so). *The recommendations:*

1. Use several agencies. Never depend on just one, no matter how good you believe that agency to be. Many firms find that using three agencies that have specific experience working with professional services firms gives them adequate coverage.

2. Don't focus entirely on fees when selecting and evaluating an agency, as prices may not translate into the highest return. Evaluate the total dollars returned to your firm at the end of the day. In fact, it's wise to be wary of fees that are much lower than the rest of the industry. Agencies that offer low fees will sometimes only make a cursory effort to collect or grab just the low-hanging fruit while leaving the really difficult accounts to others.

3. Make sure you understand the agency's fee schedule. It should be clear and easy to comprehend. If something is not obvious, ask—don't assume. Also, be aware that most agencies' fees are contingent upon their collecting something for your firm. If they are unsuccessful, they earn nothing.



4. Check references, and ask if the reference would use the agency again; how long the reference has been using the agency; and how the reference would rate the agency on a scale of one to 10, recognizing that few people will give the very top rating to anyone. Once you've made a choice, make an unannounced visit to see how the collection agency's day-to-day operations are run.

5. Verify that the agency is bonded. This will offer your firm some security in the unlikely event there is fraud on the part of the agency in handling one of your accounts.

6. Check professional association membership. Ask all prospective agencies how long they have been in business. While all new businesses need to start somewhere, your firm needn't be the very first customer.

7. Monitor results. Distribute your accounts among the agencies selected and periodically monitor the results. If one agency's record warrants it, steer a larger portion of the work in their direction. And, obviously, replace any with consistently poor results.

8. Don't wait too long before turning over delinquent accounts. Turn your accounts over to the agencies while there's still a chance of collecting. Once accounts are six months past due, they are rarely collectible—even by the best agency.

10. Negotiate a reduction for "early" accounts. Approach your agencies for a reduction in fees for all accounts turned over early. Some agencies will offer a lower rate for accounts turned over at 60 days.

11. Shop accounts around. Don't assume that because one agency can't collect on an account, nothing can be done. Some agencies will take accounts that have already been worked on by others. Of course, you should expect to pay a higher fee for this service. Since most of these agencies also work on a contingency basis, it pays to place your really bad debts with them.

12. Don't commingle collections. Make sure that your collections are held in a separate account from those of the agency. Under no circumstances should your funds be commingled with the agency's money.

When all else fails. If none of your agencies succeeds in collecting a debt, what then? Consider selling your uncollectible debts to an investor who buys debt. You won't get much—typically around five cents on the dollar—but that's better than nothing. Some buyers sit on the bad debt for a while and then try to collect after it has aged—and the debtor's financial condition has had time to improve. To find such a provider, go to www.debtbuyers.com.

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Sidebar: Third-Party Collection Agency Resources

Most third-party collection agencies belong to one of two associations:

- **Commercial Law League of America.** Top agencies have met the stiff certification standards of CLLA's Commercial Agency section and carry the desired "Certified by the Commercial Law League" designation. See the Web site: www.clla.org under "Directory" for full listings.

- **International Association of Commercial Collectors.** IACC is the world's largest international trade association for commercial collection professionals, operating in 24 nations and the U.S. IACC also currently lists 402 member agencies—238 collection agency members and 164 attorney and associate members. The listing can be accessed on the Web site: www.commercialcollector.com under "Directory."

Every "IAAC Certified Commercial Collection Agency" meets a rigorous set of membership standards, must carry a minimum of a \$10,000 statutory or blanket client bond, and is required to maintain a separate trust account for all client money.