

Problems with Payment Stretching

By Brad Schaefer, Analyst, Sageworks, Inc.

There are a few motives that explain why CFOs or Controllers may choose to stretch their payments by paying invoices past their due date. The first explanation is that they simply want to enhance their cash flow and improve the appearance of their balance sheet to make their company more attractive to investors and stakeholders. If improving liquidity is the goal, there are better ways to [enhance cash flow](#). This article will point out a few reasons why stretching payments is not a healthy practice for the business performing the stretching or for other involved parties. This sentiment is also shared by Mary Schaeffer, the author of Controller and CFO's Guide to Accounts Payable, when she expresses in her AICPA [Payment Stretching article](#) that, "the practice of payment stretching, advocated by some as a way of enhancing cash-flow, has serious pitfalls and should be avoided under most circumstances."

The other motive for stretching payments materializes from necessity. When businesses are struggling to make their payments on time, they may be forced to stretch some of their payments past the invoice due date. If this is the case, there are a few best practices that should be followed to minimize the negative effects of payment stretching that we will cover later in the article.

Delaying payments to vendors can cause several problems:

- 1. It hurts relationships with vendors.** Not only will vendors feel that they are being slighted by the company that is not paying them on time, but they will also be affected financially as many vendors are already experiencing some form of a [cash flow issue](#).
- 2. It results in duplicate payments.** When an invoice isn't paid on time, vendors will send another invoice to the company. Even with a quality system in place to track these duplicate invoices, a few will still slip through and be paid twice. As most CFOs and controllers know, these duplicate payments will rarely be tracked by the recipient of the payment.
- 3. It can cause issues internally.** More work is created for accounts payable staff as they have to manage a more complicated process (including duplicate payment prevention) and field increased calls from vendors. In addition, the extra calls will typically be undesirable money-collection calls that staff members do not enjoy answering.

As mentioned earlier, stretching payments may be more of a necessity than an option in situations where the company is [struggling with cash flow](#). Sageworks' data on privately-held companies shows that several industries have drastically increased their accounts payable days even when comparing the most recent 12 months to the prior 12 months. These industries include motorcycle, boat, and other motor vehicle dealers increasing from 15.05 to 29.86 days, turned product and screw, nut, ad bolt manufacturing increasing from 22.33 to 42.52 days, new multi-family housing construction increasing from 28.64 to 52.19 days, and boat building increasing from 26.74 to 45.10 days. Here are a few guidelines to follow to minimize the possible negative consequences of completing payments past the invoice date:

- 1. Communicate with the invoice issuer.** Inform the vendor that the payment will be late so that they know the money is coming, don't issue a second invoice, and won't be surprised when they don't receive the payment on time. The relationship with your vendor will benefit greatly from following this step even though it can be difficult to communicate openly.

- 2. Pay the invoice as soon as possible.** Some companies are tempted to withhold a payment as long as possible once it is already past due. This will cause headaches in the organization as well as negatively impact your vendor. It is best to pay the invoice as soon as the company is able.
- 3. Avoid paying the invoice twice.** Duplicate payments can be an issue for companies that stretch payments. This is especially true for companies who aren't planning on stretching payments and don't necessarily have a plan in place to catch duplicate invoices. Paying an invoice twice (once based off the original invoice and once based off the past-due invoice) will obviously further hurt your company's cash flow. As mentioned previously, duplicate invoices can often be avoided by communicating with vendors to inform them that the payment will be late.

Due to the impact on relationships with vendors, the possibility of duplicate payments, and the issues it can cause internally, stretching payments is a practice that is best to avoid. If it is necessary due to cash flow issues, remember to communicate with vendors, pay the invoice as soon as the company is able, and avoid paying the invoice twice.

About Brad Schaefer: Brad Schaefer is an Analyst at [Sageworks](#), a financial information company and developer of the [financial analysis software](#) suite for CFOs and Controllers. Schaefer has led the development and ongoing enhancement of Sageworks' credit risk management solution for financial institutions. He received his degree from the Poole College of Management at North Carolina State University where he graduated summa cum laude.

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