What Keeps Staffing Suppliers Up at Night

Your vendor's greatest concern should matter to you

By Tom Kosnik

I recently received a call from a small staffing firm that has a story to tell and a lesson to offer any customer. It is an important story about cash flow. Companies rarely concern themselves with the financial status of their staffing vendors. However, understanding issues around accounts receivable from the perspective of a staffing vendor is very important for maintaining a healthy vendor/supplier relationship.

This relatively small staffing firm was supplying professional-level temporaries to its customers on a contractual basis. Even though the bill rates to the buyer and the pay rates to its contingents were in line with market rates, the firm could not seem to find the cash in its business to grow. In fact, it was always in a cash crunch. The owner invited me to meet his staff and take a look at the business.

Discoveries

I discovered that the staffing firm's recruiters and sales reps were productive. The customers gave good reports about its services and the firm built up a fine reputation in the marketplace with contract employees. From a financial perspective, the compensation plans were not out of line with industry principles and the gross margins were actually lower than industry standards.

As we moved into discussions about the finances of the business, the person who was responsible for the cash flow took me aside. He said, "Let me tell you the trick to this business: it is financing the receivables. If we can figure out how to finance our receivables, we would be in a much better position."

I was shocked. This employee had no idea what he was doing and was putting the company, the contract employees and the customers at risk. When I dug into the financials, I knew exactly where to look. More than 80 percent of the accounts receivable were more than 60 days past due. This was a problem.

Financial Squeeze

Accounts receivable is the single most important concern from a staffing supplier's perspective. It is the issue that will keep the owners and managers at your suppliers up at night. When the receivables are running past 45 days, it puts a financial squeeze on most staffing suppliers.

Accounts receivable can be defined as the monies owed to a staffing supplier from its customers. And yes, it is critical for a staffing supplier to be in the position to fund their receivables. It is important for a customer to understand because it is a key indicator to the financial health of the business.

Why are accounts receivable such a big deal for a staffing supplier? The answer to this question, in part, lies in understanding how much

money of a staffing supplier's invoice is considered "pass through" money.

For most staffing suppliers, 70 percent to 80 percent of their total revenue is considered "pass through" dollars. Pass through dollars do not stay with the staffing supplier. For example, on a $10,000 invoice from a staffing supplier, $7,000 to $8,000 of that invoice is going to the contract workers and their direct burden (the contract workers' taxes and workers' compensation insurance).

Staffing vendors view this as financing their client's payroll. Not the entire payroll, just the payroll of the contract or temporary workers that are working at the client's site.

Let's take this a bit further. If a staffing firm with $10 million in annual revenue is averaging a 25 percent gross profit (revenue minus the contract workers' pay and burden), then the company sees some $7.5 million pass-through dollars annually. Such a company is financing an average of $144,231 a week. If the vendor's accounts receivable are running an average of 60 days, the vendor has to finance $1,153,846 of receivables.

Personal Guarantees

Most staffing firms finance their receivables through a line of credit from a bank, which will typically require the owners of the business to personally guarantee to finance any level of accounts receivable. With the previous example, the owners of the staffing vendor would be guaranteeing about $800,000 in accounts receiv-

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able as banks usually finance up to 80 percent of accounts receivable.

A staffing firm with $10 million in annual revenue is considered a small business. It is privately held and may be owned by one person or by a married couple that both work in the business. It may be a partnership.

Many of these privately held staffing vendors, are putting their homes up to personally guarantee their accounts receivable. From the owner's perspective, this is clearly a risk. You will also find that the tolerance to such risk varies from supplier to supplier. Regardless of the tolerance to risk, financing the accounts receivable is a personal thing for these firms because, for most of them, their homes are on the line.

Relationship Abuse

A company that pushes a receivable from 45 days to 60 days poses one set of concerns for a staffing supplier. The profit the supplier is making on the account decreases as there are costs to borrowing money from a bank to finance the receivables. It is more of an issue of getting the money in from the company and reducing the days in which the payable is received.

When a company pushes a receivable to — and beyond — 90 days, it becomes a whole other issue for the supplier. Many of them take it personally. From a supplier's perspective, they see it as funding the payroll of a client that is way beyond the acceptable norm. The owner starts to sweat and begins to feel that the client is consciously abusing the supplier/vendor relationship.

Pushing one's accounts receivable to such levels may cause the supplier to back out of the account. Banks will also see receivables that are near the 90 day mark as high risk. Often times, banks will tell staffing vendors to find other sources of financing these high-risk receivables.

The owner of the small staffing firm that I initially spoke about did not know what the company was doing from a financial management perspective. This is unusual. Most staffing firms understand that accounts receivable are their most important financial concern. But from a customer perspective, understanding your supplier's tolerance to financial risk and why a supplier takes it so personally when receivables go near and beyond 90 days is critical to maintaining a healthy relationship.

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