



MONEY: The Good, The Bad,



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CPA **Margaret Loh** simplifies cashflow by labelling 4 different types of money with suggestions of how to reduce your exposure to two of them and maximise the others.

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There are four types of money. There is Good Money and there is Bad Money. There is Smart Money and there is Stupid Money. If we don't know the difference, then we're likely caught in a cycle of Bad and Stupid Money. This is a bad and stupid cycle to be in.

Without knowing any more about the labels I've given them, I'm quite certain that if you had a choice, you would choose to deal only with Good Money and Smart Money. The great thing about labelling money in this way is that when the decision is on the table, if the decision is labelled a Stupid Money decision, or a Bad Money decision, the decision has been made for you: **DON'T DO IT.**

So let's explore what these are.

Usually the best way to increase good money is to do more of what brings in good money in the first place, and find out what other value you can deliver to those who pay you the good money.

Good Money

Good money is money that flows in. That could be derived from sales payments received, fees received, commission received, remuneration received, investor funds, investment dividends received, interest received, pension received, insurance returns, capital gain on property investment... pretty much any money that comes IN is Good Money. We like good money. We must find ways to increase good money. Usually the best way to increase good money is to do more of what brings in good money in the first place, and find out what other value you can deliver to those who pay you the good money.

Bad Money

Bad money is stagnant money or illiquid money, especially uncollected revenue. This means you've made a sale, but you have not collected it. It's still sitting in a receivables column (and maybe that's because of the credit term you allow) rather than in your bank account. It probably means that you have paid for the goods or services you have sold, but you have not been paid for them. This means you are worse off than if you had never delivered the goods or services in the first place.

For example if you have a net profit of \$500,000 and receivables of \$600,000, then in actual fact, your entire net profit is sitting in the receivables and your company has to operate as if you are running at a \$100,000 loss.

In the trading and retail business you may have to purchase the goods before you can sell them. Similarly, in the services business you have to pay your employee salaries regardless of whether your clients have paid you for your employees' services. So money sitting in receivables is bad money.

Goods returned are bad money. Disputes on services provided are bad money too. It essentially means returning revenue after the product or service has been delivered and paid for by you.

The Smart & The Stupid

Avoid giving refunds. The revenue refunded usually includes the cost of goods sold plus a portion of operating expenses and a portion of profit. Give replacement or substitute products or services if you can, because this lets you keep the operating expenses and profit that you earned. And of course fix the problem that caused the refund. If you notice it is a refund-hungry customer, then stop doing business with that customer.

Bad debts are of course bad money. It is money that cannot be recovered. Often this is the result of waiting too long to try to collect revenues, or a business going out of business. Somewhat cynically perhaps, it what money lent to a family member tends to become. Kiss it goodbye. Bad debts are

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an indicator of poor lending decisions and criteria. These can be the conditions upon which credit terms are given to customers, an investigation of their capacity to pay, the collection timeframes and the course of action to pursue before the borrowers payment capacity completely dries up (they go out of business, for example).

Bad money also includes additional funds from shareholders. This usually means two things. Either the way the business is being run is not generating enough of a return to sustain it (so the shareholder needs to add funds to keep it afloat), or the business is expanding too quickly to pay for its own expansion and thus needs a "short term capital injection" to deliver a more sizable result. Both are bad money.

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If the business expansion cannot be paid for out of direct or leveraged reserves or through obtaining external funding other than additional shareholder funds, then there is something questionable about the expansion. Perhaps the

expansion seeks to operate in another location because the way it was poorly run in this location was blamed on the location rather than the way it was run.

Loans from banks means interest is payable on the loans. Paying interest is bad money. You have much better things to do with your money than paying interest with it. It needs to be minimised or eliminated as soon as possible. Some may argue that it is better to use borrowed money from banks than use your own money. If you're borrowing to pay expenses then it is bad money. Banks will require collateral and guarantors for the money, and so you're not only taking the risk on the borrowing but you're tying up your assets as collateral to borrow for non-profit-generating items. No ROI equals bad money.

Stupid Money

Overspending is stupid money. This is when you pay more for something than you need to, or paying more for things than you have. It includes incorrect expenditure, such as buying the wrong things, unjustified expenses, which includes paying for things that do not give you a measureable return for





having bought it.

It also includes paying for things before you need to. For example, you have 30 days credit terms but you pay cash on delivery (COD). Or you assume COD but you could have negotiated terms. Paying early, while noble, is stupid. It's tantamount to paying before you get paid.

Poor processes that waste money are very stupid. But buying a super-automated process enhancer that never returns you its purchase and operating costs is even more stupid. Often all it takes is some effective planning, the identification of transactions that can be streamlined and process points that can be eliminated, and some appropriate reports and analysis to indicate areas of improvement. Ask for help if you have to, have a fresh pair of eyes question your practices. If you can't give them a good answer, don't defend the practice, target it for elimination or improvement.

Heavy administration is stupid money. Unless people pay you for administration, do whatever you can to streamline it and reduce the costs associated with it. Maybe find someone whose business is to do administration. If they can do it more cost effectively than you without any loss in quality, compliance or security, outsource it to them.

Smart Money

So now let's look at smart money. Being paid before you perform, and paying later than you purchase, is smart. Legally using someone else's money is smart. Get deposits from customers, or bigger deposits from customers. This means being paid in advance. If you can get all of it in advance, then that's the best. Getting paid before you do anything is smart, as you'll never have any bad debts that way. So we're eliminating bad money.

Negotiate generous supplier credit terms. This means you get to defer your payment to them for longer.

Paying your supplier before your customer pays you is not smart. Ensure your payments terms for what you purchase are longer than your receivable terms for what you sell. The best is to have lengthy credit terms with your suppliers and 100% pre-payment from your customers.

Smart Sales produces Smart Money. Sell first, collect the deposit, then commence production after you have the initial funds from deposit collected. The construction industry uses this well when building a house or developing a condominium. They sell the buildings with drawings, plans, scaled models and display homes. Another example of Smart Money is from the sales of licenses, certifications, accreditations, rights and royalties to research and develop technologies. This is selling a standard. It's not even a product or a service, although sales of those come with the consulting, training and assessments that support the pursuit of being awarded the sought after proof of standard.

Now I had earlier mentioned that Loans from banks was bad money, because you have to pay interest. In fact, Loans



from banks can be smart money too so long as the money generated by the loan is larger than the interest paid to the bank. When borrowing to generate revenue (Good Money) that is greater than interest payable (Bad Money) then the borrowed amount, and its associated terms, is an example of Smart Money. Borrowed money is essentially using someone else's money. Using other people's money, with their permission, to make you more money than the cost of that permission, is clearly smarter than using your own money. That's because no matter how you look at it, the sum of everyone else's money will always be greater than the sum of your own money. So you can do, and earn, so much more with theirs than yours. The only caveat is that you know what you're doing. Otherwise you're just gambling.

Account Ability

So pursue Good Money and Smart Money. Engage in Smart Sales. Eliminate Bad Money and Stupid Money. With great money comes great accountability. Because without the ability to account for your actions in spending and earning, you won't have the great money for very long. Those who have too much bad money and stupid money in their business will continue to struggle until they recognise their need for additional financial development. Develop more account-ability. That's good and smart business.

P.S. There is actually a 5th type of money, Safe Money but perhaps I'll save that for another time. 🍷