MANAGING WORKING CAPITAL

In the fifth of his series on GP financial management, accountant Ian Tongue explains the mysteries of working capital and its importance to general practice today

Working capital is the name given to the short-term assets and liabilities of the practice. As they are short term they generally require more time and effort to manage effectively, but this does improve the cash flow of the practice.

What is working capital?

Working capital consists of the items shown under the current assets and liabilities section in the surgery's balance sheet. Typically these comprise:

- cash in the bank
- cash in deposit accounts
- stock
- debtors
- creditors
- overdrafts.

Each of these areas will require a strategy to ensure the interaction between them produces the optimum flow of cash into the surgery.

Cash management

Policies for the retention of cash will vary between surgeries, depending on factors such as whether the doctors' personal income tax liabilities are paid by the practice. However, all practices should ensure they have sufficient funds to pay day-to-day operational expenses.

The current account usually pays a very low rate of interest and therefore its balance should be minimised and deposit accounts used for surplus funds. The traditional methods of cheque or online transfer are the favoured methods of moving surplus funds from the current account. Facilities to 'clear down' surplus funds should be avoided as they can make accounting for the transfers overly complex.

Stock

Stock management is an area that is often overlooked and is an issue for every practice, not just those that are dispensing.

Controlling who is able to order drugs and medical supplies can prevent items being ordered in error and in some cases being disposed of as they are past their useful life. Carrying excessive stock reduces the amount of available cash as the surgery has effectively 'invested' some of its available cash.

Ideally, a surgery should only have on hand what it requires and should only order items when they are needed.

Debtors

This is the key area where significant improvements to cash flow can be achieved. A modern GP surgery has many income sources and it is important that these are constantly monitored.

Many aspects of a surgery's income are claimed and are usually received in arrears. This means the surgery should focus on ensuring all claims represent the complete range of services provided and that payment is received as soon as possible.

The key areas where improvements can be made are:

- enhanced services
- drug claims
- trainee reimbursements
- prescribing incentives.

The most important aspect of managing the above is awareness of what the surgery can claim for and what is available to the practice.

With the various day-to-day pressures that practices face it is easy to let claims fall behind. But this adversely affects the cash flow of the practice.

At present, GP surgeries are experiencing stagnating or reducing income and rising costs. Therefore not managing claims is tantamount to giving away practice profits.

Creditors

Managing the amount owed to external suppliers and other parties is also crucial. It is important to make the most of credit terms offered by suppliers. If a supplier offers 60 days' credit, why not use it to the full? Also, the prices paid for goods and services can vary widely and it is important to make someone responsible for ensuring that the best deal is being obtained. There are specialist companies and organisations around to assist in procuring goods and services, such as First Practice Management.

It is not uncommon to see practices paying bills early, such as the monthly PAYE and National Insurance bill – many settle these in the same month that the salaries are paid. However, the payment is not due until halfway through the following month.

HM Revenue and Customs does not offer interest-free credit often, so use it the full! Likewise, if the surgery pays the income tax for the partners, pay it as close to the due date as possible.

Overdrafts

An overdraft is usually the first port of call when there are cash flow difficulties and they can be useful as a temporary measure given the timing of certain cash flows in a practice, for example QOF payments. However, care should be exercised as the interest rates on overdrafts are generally much higher than other types of loans. Using an overdraft to pay excessive drawings, for instance, is a false economy.

Reliance on overdrafts can often be a sign that the funding of the practice by the GPs is insufficient. Ideally, GPs should set a minimum amount for their current accounts which will broadly equate to the practice's normal funding requirements.

Each practice will face different financial circumstances. However, it is important that the practice identifies how much funding or 'working capital' it requires and how each part will be managed. But practices can no longer ignore working capital management.

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