

business management

The bank – the business partner you can't do without

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Banks have two primary functions. Firstly, to provide finance and secondly, to help you manage the day-to-day dealings of your business by providing your current account, deposit accounts and short-term borrowing facilities, such as overdrafts, stocking loans and credit card accounts.

The current account – the basics

The current account acts as the main point of contact between you, your business and the bank. The account has a fairly complete record of how much money came in (usually income from sales or direct payments) and how much was paid out to meet the running costs of the business and your personal drawings.

Banks refer to the current account as the “track record” of a customer’s dealings with them. More importantly, you can also make use of your own bank account data to help manage day-to-day cashflow and track spending.

Using a cashier in a bank branch to lodge a cheque or cash or to make a withdrawal is becoming more expensive as a result of transaction charges and is less convenient, as cashiers become rarer than hens’ teeth.

Farm businesses are increasingly using modern direct debits, standing orders, on-demand electronic transfers, mobile or internet banking, credit cards and debit cards.

All of these methods of transferring funds usually cost less in bank charges and allow speedier movement of funds between accounts.

Standing order (SO) v direct debit (DD) – what’s the difference?

A standing order is set up by the bank account holder to create an ongoing (for example, every week or month) transfer of a fixed amount of money to another bank account. To set one up, you need the bank account details of the receiving bank – the bank identifier code (BIC) and international bank account number (IBAN).

Most online banking systems allow you to set up standing orders your-



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self, so you can easily move money between your own accounts – such as from your current account to a deposit account for regular savings.

A direct debit is a request from another bank account for the transfer of a variable amount of money from your account. It requires that you have pre-authorized this transfer, but rather than being initiated from your account (as with a standing order), the order to transfer funds comes from the payee’s account.

The organisation requesting the transfer must issue you with an invoice a number of weeks in advance of the direct debit so that you have a chance to query the payment before it is made.

The bank charges, but also the taxes imposed by Government on financial transactions, are all encouraging less cash and cheque transactions and more electronic or card transactions.

From 1 January 2016, there was a change in the charge for withdrawing cash from a “hole-in-the-wall” ATM as 12cents stamp duty is levied on each use of a card to withdraw cash – subject to a maximum yearly charge of €2.50. Electronic transfers usually still incur transaction charges, imposed by the bank, and stamp duty charges, such as the annual charge on the use of credit or debit cards.

These stamp duty charges are much less in that there is usually just an annual charge for the use of a credit or debit card, rather than the current stamp duty of €0.50 on each and every cheque.

Many people still prefer using cheques, as it allows them to record the details of the transaction on the stub. They feel it will be easier to categorise the expense for accounts purposes.

But online transfers of money also allow you to add a message or further information to a transaction, so that

you can trace what it was for at a future date.

Become account vigilant

As electronic payments increase, it becomes more important than ever to monitor your business’s current account. Many businesses still receive a monthly bank statement on paper, although some banks incentivise customers to move to an electronic statement received via email or viewed online.

It is a good idea to “check in” with your current account more than once a month.

- What is your balance? Is it around what you would expect?
- Do you know what all the various transactions (transfers in and out) listed for the account were for?
- Can you see what future transfers are pending (due to happen in the next month) and will there be funds there to meet them?

Online and mobile banking has improved a lot with screens that are easier to navigate around and there’s a lot more options to use to help manage your accounts.

You can group transactions together by category (using the description attached to the electronic transactions) and search for a specific cheque by number or date.

Apart from monitoring your current account it is also a good idea to check, at least once a year, the total debt on the business. A simple list of all the debts with the main terms and interest rates will focus the mind on how to manage the current debt, as well as assisting in decisions about taking on additional loans to fund new investments.

The golden rules of current account management

Never write cheques for amounts that exceed the account balance plus maximum overdraft facility – if there is one. Regularly incurring referral fees due to unpaid direct debits or bounced cheques is seen by the bank as an indication of your inability to properly manage cashflow.

Similarly, not abiding by conditions such as bringing the current account back into the black for at least 30 days during the year is seen as a black mark on your current account track record.

Figure 1: A useful table to help monitor your debt

	Loan Name/ Lender	Initial Amount Borrowed	Initial Loan Term (years)	Current Amount Outstanding	Rem aining Loan Term (years)	Current Interest Rate	Total Repaym ent per year
<i>Example</i>	<i>Land Purchase Loan / Z Bank</i>	€120,000	<i>12 yr</i>	€84,800	<i>7 yr 9 mth</i>	<i>6.70%</i>	€14,868
Term Loans (incl house mortgage)		€		€		%	€
		€		€		%	€
		€		€		%	€
		€		€		%	€
Stocking Loans		€		€		%	€
		€		€		%	€
		€		€		%	€
Hire Purchase/ Finance		€		€		%	€
		€		€		%	€
		€		€		%	€
		€		€		%	€
Overdraft		€		€		%	€
		€		€		%	€
Merchant Credit		€		€		%	€
		€		€		%	€
		€		€		%	€
		€		€		%	€
Other		€		€		%	€
	TOTALS			€			€

You can help avoid this by keeping the overdraft facility exclusively for meeting short-term demands for funds such as the regular running costs of the business, rather than spending it on large outlays.

These might include spending on large-sum investments, such as buildings or machinery, which usually don't generate enough income in the short-term to recharge the account with funds.

Apart from tarnishing your account management record, exceeding the overdraft means you can end up paying surcharge interest on top of the substantial overdraft interest rate.

Preparing a loan application

Another very useful support that banks offer is to assist businesses in financing large investments. There is scope to negotiate rates, but the bank will work through a formula to set its rate after assessing the risk and the repayment capacity.

Most banks price their interest rates based on a margin over the "cost of funds" – i.e. what it costs them to borrow the money on the money markets.

Calculating a borrower's repayment capacity involves assessing the amount of free cash that the business potentially has available to make

repayments on the new borrowings. The following formula gives an idea of how this repayment capacity is calculated in practice:

Calculating repayment capacity

Net Profit (from accounts or eProfit Monitor).

Plus Non cash deductions (e.g. inventory change, depreciation charged).

Less Living expenses (household running costs, pension and health insurance payments).

Less Expected Income Tax to be paid.

Less Principal to be repaid on current loans (the interest fraction is already deducted in the calculation of net profit).

Less Annual cash spend to fund small investments and other outlays

Equals Free Cash available to make repayments on new loans.

Apart from repayment capacity, the bank will also look at your previous track record at managing your current account (as outlined earlier), the amount of your own funds you will be contributing to the investment and the security you have available.

A detailed loan application form will supply the bank with much of the information they need, but ad-

ditional information can also be used to support an application.

Banks are now routinely requesting three years of tax accounts, eProfit Monitor reports and ICBF reports, if available, to help give a picture of the farm financial and production characteristics.

Projected cashflows for three to five years with a projected balance sheet for the same period can also be useful to demonstrate to the bank that the investment is going to have a positive effect on the financial status of the business over the term of the loan.

The bank uses these projections to satisfy itself that the loan can be repaid and the business can still meet its other obligations over the term of the loan. Stress-testing these cashflows by assessing the effect of higher interest rates and lower prices for sales product are also routinely carried out by the bank.

For any business looking to avail of bank finance, it is worthwhile preparing well and having a clear idea of what the loan will be used for and what effect it will have on your business. Backing this up with well-prepared financial projections (cashflows) can greatly help in getting the best deal and best terms possible from the bank.