Ebook

Six Key Metrics for Professional Services Organisations

Calculations, obstacles, and best six key practices for financial excellence

kinspeed
Forward thinking. Industry leading.

Sage Partner

Table of contents

kinspeed
Forward thinking. Industry leading.

Introduction

Service Performance Insight conducted a recent survey of 622 professional services organisations ranging from IT Consulting, Management Consulting, Marketing, Accounting, Legal and other types of service-based businesses, that has helped shed new light on performance expectations in a number of key areas*. These Key Performance Indicators (KPIs), can help organisations benchmark their financial data, and identify where they need to focus as they strive for continuous improvement and growth.

This whitepaper will highlight the latest actionable KPIs and discuss the factors that commonly affect these numbers and what you can do to improve them. We will also provide real world stories of financial leaders that have faced these challenges and found ways to succeed.

Cash flow—reissuing invoices

Let's talk about cash flow. While cash flow encompasses money coming in and money going out, for our purposes, let's focus on the money coming in.

Reissuing invoices due to invoicing errors can have massive consequences on your cash flow. Calculating your reissue rate is as simple as taking the number of reissued invoices divided by the total number of invoices sent. Data shows that 25% of all companies surveyed, needed to reissue over 3% of all of their invoices annually. For those companies, the impact of such a high reissue rate resulted in nearly 5% more project cost overruns and a 7% reduction in their ability to deliver projects on schedule*.

Common causes of reissuing invoices can include time coding errors, and fees that were not in the agreed upon contract. Often times, timesheets are difficult to use, disconnected from the accounting software, or completed long after the work was done.

Employees can commonly forget time, put time in the wrong place, or add the wrong employment code. If the project manager doesn't catch it, your customer will. Another challenge comes when the customer disputes the charges due to poor communication, confusing invoice, or a flawed schedule of work.

You can work to improve this KPI by ensuring that your team enters time daily, and they are only able to enter time to active tasks or tasks where they have been assigned. Use a billing system that recognises your contract amounts, and provides detailed project, task and resource status information that can help simplify the time entry process for your team. If you have a system that is built for all types of project-based companies, you should be able to enforce daily time entry using alerts and visibility for your supervisors.

Case study

Berkshire Associates struggled with a complex billing system while trying to bill for fixed fee, time, and subscription customers. By switching to Sage Intacct, they were able to take advantage of a project-based accounting system and cut their invoice cycle in half.

"In the five years since we graduated to Sage Intacct, our revenue increased significantly, and there's no way we could've kept up with that growth if we were still using QuickBooks. I used to work up to 80 hours a week, but now I work 40-hour weeks with the same-sized team, thanks to the amazing automation and productivity boost we gained with Sage Intacct."

Lisa Roeder, Business Manager, Berkshire Associates

kinspeed
Forward thinking. Industry leading.

Cash flow—billing cycle

"Because of our integrated solution, we're able to forecast our cash with a fair bit of precision, and that's pretty phenomenal because cash is one of the hardest things to forecast."

Corinne Hua, CFO

There's much more that impacts cash flow than just reissuing invoices. Your overall billing cycle starting with the moment your cost is incurred and ending with your cash receipt, can also have significant impact on the financial health of your business.

If you bill monthly, as most service companies do, you can imagine incurring an expense or employment cost on the 1st of the month, billing for it on the 30th and collecting for it another 30 to 45 days later. That doesn't include any challenges you have to getting your bills out the door. Many companies take 5 to 10 additional days just to prep the invoices to send to their customers.

The cost accumulation throughout the month is commonly referred to as Work in Progress (WIP). WIP is an asset since it's billable, and if you track it you generally clear it out every time you bill for it. If your cost accumulation is fairly uniform throughout the month then you can estimate your WIP ageing to be 15 days, add that to your average days to get the bills out the door after the end of the billing cycle, then add that to your average AR days ageing.

Common causes of lengthy billing cycles can be late time entry, adjustments, long project manager review processes and complex invoices that are manually created. Depending on the complexity of your billing process, it can take anywhere from 5 to 10 days to get your bills out the door.

Disconnected or generic accounting systems are very difficult on the billing process for service organisations because they often lack billing functionality that is capable of the heavy lifting required. It can be impossible to grow your business, and this is often the primary bottle neck administrative teams face as they scale.

If you are using a disconnected or generic accounting system, there is very little you can do to fix the billing cycle. You need to work with an accounting system that is built to handle complex project accounting and billing requirements. Once you have system with the features you need, you can reduce things like the lengthy approval process by providing real-time project financial data to your Project Managers so they already know what will be on the invoice and have taken action on time entry errors.

You can also create a purely digital invoice review process with alerts to keep your managers on task and create an audit trail of any invoice change requests. Your ability to create even the most complex invoices should be solved with the right financial system, allowing you to invoice faster, and grow your business. Reducing your billing cycle provides very tangible benefits. If a company has £23 million in annual revenue with an average billing cycle (not including WIP ageing) of 45 days and they reduce by 10% to 40 days, that can create up to £317,000 in additional cash on hand. That improves your value, ability to secure any loans, and overall increases your financial flexibility.

Case Study

Traction on Demand was entering a phase of significant growth, expanding from 150 to 500 employees. They needed a more connected system to automate project billing to keep pace with the heavy workload. With Sage Intacct, they were able to connect their systems and reduce administrative burden on the monthly billing process.

kinspeed
Forward thinking. Industry leading.

Cash flow—collections

After you've invoiced your customer it becomes a waiting game for payment. Most companies will have scheduled email reminders or phone calls to ensure payment at 15, 30 and 45 days.

There is also language regarding payment in the customer contract that specifies terms and timelines. With all that in place, it can still be difficult to collect. Many companies don't track their AR ageing (also known as Days Sales Outstand – DSO). DSO is a simple calculation of your total revenue for the year divided by 365 to get your daily revenue, then divide that by your AR balance at the end of the year and you get the average number of days from billing to payment.

While the recent survey noted an average of 45 days for DSO,* that number can vary wildly depending on the specific type of work you do. Let's focus on what impacts that number and what you can do to improve it.

The longer the collections process takes, the more likely there will be bad debt, write-offs and strains on your financial health. Common causes to delayed collections are billing disputes, clarifications and customers that just like to wait until the last minute to pay. It seems like there is little you can do to improve this process but that's not the case.

You can find ways to improve the collections process. Many organisations will offer incentives to their customers for paying early, such as 2% off (commonly referred to as 2/10 Net 30). Incentives are nice, but they can defeat the purpose of adding to your cash flow. Ensure your contract has timelines that make sense for you. Try switching from 30 days to 14 or even 10. If you're dealing with a large company, try to understand their standard payment process and invoice them just before they cut their AP cheques.

Case Study

Creative Dining was struggling with visibility into the fundamentals of their business, and was stuck with gruelling manual data management. Switching to Sage Intacct allowed them to become strategic in their operations, and provide AR specific dashboards to their business units to reduce their collections time.

"We're seeing massive savings due to the automation we've accomplished with Sage Intacct. And rather than crunching numbers all day, we are seen as strategic business advisors to our client location units."

Jeff Banasza, CFO

kinspeed
Forward thinking. Industry leading.

* Service Performance Insight 2019 Professional Services Maturity Benchmark Report

Utilisation

Utilisation is the single most used metric of any Professional Services organisation that needs to track time entry.

Over the years, business leaders have heavily focused on ways to maximise the utilisation of their teams, given its direct impact to the bottom line. Survey results put the average utilisation at about 70% with year to year fluctuations within 1% to 2%.* The type of organisation can have more impact on this number. For example, VAR and software implementation teams tend to see lower utilisation (closer to 65%) due to high write-offs, rework and low bids to win lucrative software contracts.

A common issue for smaller firms is they just don't track time very well. In many cases their timesheets are disconnected from the accounting system making it difficult to measure and improve. They also tend to struggle to track any details regarding their time entry.

Another issue can be the regularity that time is entered, basically the longer it takes to fill out the timesheet, the more likely it will be missing time that should be billable. Time entry needs to be done daily. You should also track every bit of time that your employees are 'on the job'. That means tracking time when they are training and working on administrative tasks.

Making improvements here starts with accurate measurement. Once you have that, you can take steps to ensure time entry is easy and billable events are not missed.

Case Study

Halloran consulting was flying blind with understanding their time entry as they worked through a busy work schedule. By switching to Sage Intacct, they were able to get a comprehensive view into their professional team's output and drive strategies that resulted in an 18% increase in utilisation.

"Before, we were stuck in the day-to-day weeds of closing the month. We'd get two days to breathe after the close, but couldn't analyse the data or get new projects done—there was no time. Now I can look at my dashboards and reports and know that the data is solid and literally up to the minute."

Tania Zieja, CFO

* Service Performance Insight 2019 Professional Services Maturity Benchmark Report

Write-offs (revenue leakage)

Write-offs should be closely monitored for any service-based organisation. Things like disputed charges, rework and discounting can all have massive impact on the bottom line.

Based on survey data, average revenue leakage sits at about 4.3%*. That is very high. It's difficult to say how much of this is related to discounting services up front, but it is common for service teams to start a project knowing that it was underbid. This number can range based on the type of service you deliver. For example, software implementation teams averaged over 6% revenue leakage, while management consulting averaged just over 3.3%*.

Revenue leakage is identified as revenue that was earned but not realised. It can be difficult to fully grasp because some contributing factors can happen at the timesheet level with entries that were missed, or not entered because you knew that it wouldn't be billed. To see how you stack up, you can simply compare your write-offs to your employment revenue. It's important that you are still capturing all your billable revenue and then writing it off if you can't bill it.

If you change that revenue to a non-billable type transaction, or don't account for it at all, you can drastically change your reporting. Keep things that are actually non-billable activities separate from things that are billable, even if you know it will be written off. That way you know your true project performance and you can accurately bid future jobs.

Revenue leakage is most commonly blamed on under bidding contracts. That means that projects tend to start off on the wrong track. Rework is the other primary driver of this number. Writeoffs are common when there is a dispute between the service provider and the customer.

Typically, the service provider feels it is best to provide some amount of additional work to satisfy the customers displeasure. The best way to reduce your revenue leakage is very straight forward. Quote your projects based on past project performance, not past contracts. And, don't be afraid to bill your customer for additional work that results from a change, no matter how small. All of this should be clearly discussed in the beginning stages of the contract. While you do need to balance winning jobs and customer satisfaction, make sure you're not doing it at the expense of your company profits.

Case Study

Colmore had legacy solutions and inherited processes meant long-winded and fiddly manual process were hindering the way Colmore PS wanted to operate. The company needed a simple way to create a centralised financial data repository with increased flexibility and more automation.

"Sage Intacct had the functionality we were looking for around consolidations, multi-entity and multi-currency; and it's good value for money."

Andy McKeon, Group Financial Controller

kinspeed
Forward thinking. Industry leading.

* Service Performance Insight 2019 Professional Services Maturity Benchmark Report

Project profit

Project profit is the most tracked KPI for service-based companies. Survey results put the average project margin at about 35% but again this can vary depending on the type of service you provide.

It can also correlate to your access to information. SPI noted a 9% difference in profitability between companies that reported having access to real-time project costing and those that did not.*

Surprisingly, not everyone tracks project profit the same way. For many, it comes down to how you calculate your employment cost for salaried employees. If they work more than 40 hours in a given week, do you reduce their cost against your project? Some people do, while others will use a standard cost rate regardless of hours worked in a period. Using a standard cost will add a payroll variance to your ledger but that's a small price to pay for realtime project costing data.

Using effective costs should be done with caution due to the challenges of historical reporting as well as other cost adjustment issues that result from recalculating cost after you run payroll.

Project profit can be affected by a number of factors. Project managers have a tendency to complete 80% of the project work with the remaining 20% of the budget. The primary hit to project profit comes from under bidding at the beginning and then comping work as customer disputes inevitably arise. Another factor can be delayed or inaccurate time entry.

Late timesheets can cause project managers to make project decisions based on the thought of having more room to work with in the budget. Late timesheets are also more error prone, which may not impact the project's profit, but you do miss billable time and reduce potential revenue, as well as introduce some of the cash flow issues mentioned above.

The best way to ensure you are optimising your project performance is to provide real-time project costing to your project managers and review these reports regularly with your team. Of course, just tracking the accumulating cost isn't enough, you should be tracking the actual percentage of completion on the project and its tasks to the lowest level of effort that makes sense. Some of the most advanced project tracking can
be done with a detailed analysis of what you've earned by percent complete, compared to what you've spent to date.

If you take those metrics and add the aspect of expected delivery time, then you have a very powerful project management model, commonly referred to as Earned Value Analysis. Consistency and visibility are the key to project success.

Case Study

Halloran consulting was using a combination of QuickBooks and NetSuite's OpenAir to manage their project work. As a result, the project costing data was disconnected and out of sync. By switching to Sage Intacct, they were able to get their project managers real-time data, and drive higher project profit.

"We really hit it out of the park last year because we were able to see real-time data. Any time we saw things going south, we were able to react really quickly rather than waiting until the quarter was done."

Tania Zieja, CFO

kinspeed
Forward thinking. Industry leading.

* Service Performance Insight 2019 Professional Services Maturity Benchmark Report

About Sage Intacct

Sage Intacct is a best-in-class financial management solution. Over 1.5 million projects are run on Sage Intacct for a variety of organisations including consulting, BioTech, marketing, technology, accounting and more. Sage Intacct streamlines project accounting, while delivering real-time budget vs actual visibility for project managers, and detailed financial reporting for finance teams.

Our modern, true cloud solution, with open APIs, gives projectbased businesses the connectivity, visibility and efficiency they need to drive project performance. At Sage Intacct, we help service organisations strategically grow their business through detailed insights to support critical decisions.

kinspeed
Forward thinking. Industry leading.

kinspeed

Forward thinking. Industry leading.

Sage Partner