

Factors

BY BOB REISS

Long-time friend of MANA Bob Reiss has graciously allowed *Agency Sales* magazine to serialize his book *Bootstrapping 101: Tips to Build Your Business with Limited Cash and Free Outside Help*, available now on Amazon.com. The book looks at surprisingly effective low-cost and no-cost ways to acquire the resources you need to run your company. Whether your company is an existing enterprise or a start up, a manufacturers' representative company or a manufacturer, this book will introduce you to innovative ways to cut your costs and drive more of your income into bottom line profits.





Factors finance \$120 billion in receivables, yet most small and start-up businesses are not aware of them. Business schools rarely acknowledge them. However, they can alleviate your cash flow problems.

They can lend you or advance you money against your receivables and, in some cases, against your inventory.

In other words, your receivables are an asset that the lender (factor) purchases.

The Advantages of Using Factors

- You get payment for your invoices within days. This allows you to pay your suppliers on time and thus build up your trust factor with them and to take advantage of their cash discounts. It is a financial tool that speeds your business' cash flow.
- All your costs are variable.
- Factors check the credit of all your customers and would-be ones. Thus, you get more accurate and current information than if you performed this function on your own. Also, more money is saved by eliminating the need to hire a credit checker, and you eliminate your bad debts.
- Factors collect all your receivables. In today's world, the majority of customers like to stall the payment of their bills. Some will not pay until someone calls them

The factor is only interested in your customers' credit rating.

for payment. The factors have more leverage than you as an individual have. They may represent 50 suppliers of one customer. A number of years ago, one of the biggest retailers in the country was terribly late in paying their bills and in communicating their reasons for so doing. So, the factor with one stroke told all 50 suppliers to cease shipping to this account at once. Needless to say, the CEO of the company immediately got involved, and the checks started flowing again.

- Factors act as insurers of the receivable. If after you ship a customer and the customer goes bankrupt, the factor may be stuck, depending on your contract, not you. This feature can help you sleep better.
- The factor can take over some of your administrative functions and save you the resultant labor costs. On one of our game companies that was created around a licensed product, the factor supplied us with data on monthly shipments which acted as our Royalty statement. They also provided us with total shipments by territory or account which we used as our sales rep commission statements.
- You can get money even though you don't have a good credit rating. The factor is only interested in your customers' credit rating.

The Disadvantages of a Factor

- You have a cost for their services, albeit a variable one. Fees can be from two percent to seven percent of invoice value. The amount varies based on the credit quality of your customers, the revenue you generate, the

Three General Types of Factoring

1. Regular Factors

Regular factors will advance you money on the receivables (not the purchase orders) of approved credit worthy accounts (in their opinion). This amount is usually 70-90 percent of your receivables.

2. Asset Based Lenders

Asset based lenders will loan you money based on your receivables. Many banks fall into this category. Be aware that this method does not insure you against default of your receivable. Also, you must do your own credit checking and collecting.

3. Purchase Order Financing

Purchase order financing is a very small part of the industry. Money is advanced to your manufacturer or exporter, based on your customer's purchase order. The purchase order financier works hand in hand with a factor, who then takes over the loan when goods are received in a warehouse. This financing method is more for larger companies.

You need to thoroughly read the factoring contract to understand all fees and potential ones.



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health and reputation of your company, and the time it took for your customer to pay the receivable. You should realize that the annualized interest rate in the industry runs 24-36 percent. The offset of these fees is the savings you generate from some of their advantages. Also, this is often the best of your options; certainly bank loans — if you can get them — are cheaper. Venture money, if available to you, comes with your giving up equity and possible control.

- Some factors may alienate your customers with their harsh collection tactics. If this is a problem that you can't resolve with them, then you can take over the collection process.
- You need to thoroughly read the factoring contract to understand all fees and potential ones.

Once you find the appropriate factor for you, then all shipments must be approved before you can ship to a customer. Also the factor will tell you the maximum dollar amount you can ship to a particular customer. The best way to handle this is to supply the factor with a list of customers you plan to sell. The factor will, in advance, inform you which companies you can sell and up to what amount. If they don't approve a customer, then you are on your own with that account, and you will get no money for its receivables from the factor.

How do you locate the appropriate factor for you? First I would suggest doing an Internet search for factors in your area. You also could contact your local SCORE (Service Corps of Retired Executives) or SBDC (Small Business Development Centers) chapter. You could also

contact your banker if you have one. Another very good source for you is the International Factoring Association. Their website is www.factoring.org. Click on Factor Search, fill out their form, and they will match you up with appropriate factors for your needs. All members of the IFA have agreed to adhere to the IFA's strict code of ethics.

You will find many times in your company's life that a factor can be the answer to your cash needs. This is particularly true in a fast growth situation where your money gets tied up in receivables and inventory.

Factoring is an option you should know about and understand.

MANA welcomes your comments on this article. Write to us at mana@manaonline.org.

Bob Reiss was a national manufacturers' representative for 14 years before changing his business model and becoming a manufacturer who sold through manufacturers' reps. He has been involved in 16 start-ups and one of his companies was named to the *Inc.* 500 list of America's fastest-growing companies for three years in a row. A native of Brooklyn, New York, he is a graduate of Columbia University and Harvard Business School. An army veteran, he is the author of *Bootstrapping 101 — Tips to Build Your Business With Limited Cash and Free Outside Help* and *Sales Reps*, both available now on Amazon.com.

