

# ANATOMY OF A BROKERED DEAL



## Submitting Your First Deals



### NOTES

Being a factoring consultant means you need to acquire a broad base of knowledge regarding your product areas. Textbook definitions of financing terms are great but as you begin to develop leads and prospects, the inevitable “How does it work?” question will be asked a thousand times. So, in order to answer confidently, you need to know a little more about how you submit business to a factor, how your submission is underwritten, and how the subsequent daily operations necessary to provide your client with factoring services work.

Some great news here is that submitting a prospective client to a factor almost could not be simpler. Once you’ve located an interested business owner through your marketing efforts, there will only be one completed form necessary to submit your deal. That form is called a *Company Profile*.

A Company Profile (download PDF in the *Campus*) is a 2-3 page document which provides some “quick look” background info for a factor to determine whether the client and the client’s industry is suitable for the factor’s portfolio. Or in other words, is it a match?

### COMPANY PROFILE



As an independent broker, you have absolutely no contracting or additional document duties. In fact, almost anything else you provide at submission will simply be duplicated when the factor begins its own due diligence process and underwrites the deal. Your freelance brokering business is strictly one of lead generation and qualifying. Nothing more and nothing less.

## Where to Submit Your Deal

Once you have a completed *company profile*, you will need to call upon your newly acquired broker skills to determine exactly where to send it for financing. As discussed in the last chapter, there are hundreds of what we would term “plain vanilla” factors who will always be happy to look at your deals. If your deal involves a *niche area* of factoring, such as construction, you need to make certain you send the deal to a factor who provides services in that specialty industry area.

## Analyzing the Company Profile

When you receive a completed *company profile*, you will need to perform some initial analysis of the submission to determine if it is a valid deal that deserves your attention or one which represents an impossible task. As you know, asset-based finance is all about collateral. If a true collateral exists, there is probably a way to finance it. If no collateral exists, there are few options for funding and factoring certainly isn't one of them. Below are some items to check, areas of concern, and questions to ask your prospect based on an initial profile submission.

- **LEGAL DESCRIPTION:** View the legal name of the business and check it at the Secretary of State's website in the client's state of operation or incorporation. If a corporation or LLC, it should be “ACTIVE”. If not, tell the client the status must be updated to “ACTIVE”. While not 100% necessary for you to do this, this addition to your submission package makes it and you look a little more professional to the factor. Print the results of your legal description search and include it along with the *company profile* when you submit the deal.

**ANALYZE THE  
PROFILE**

- **BANK LOANS OUTSTANDING:** As you know, your factor will require a senior secured 1st lien position in accounts receivable in order for a factoring arrangement to be put in place. If bank loans are evidenced on the *Company Profile*, talk to your prospect to determine the purpose of the loan. Does it involve real estate, vehicles, equipment, or is it a line of credit?

**NOTES**

If the loan is a business line of credit, it is likely that the bank has a *blanket lien* with "all assets" of the business pledged to secure the loan. If a loan balance is not included on the Company Profile, ask the business owner the approximate loan balance and what the loan is for. If you are in a state that provides free UCC searches, you can pull the UCC filing and view the financing statement.

Additionally, do not be surprised if an outstanding loan is not referenced at all on the Company Profile. Many business owners are unaware that a UCC Financing Statement has even been filed on what they may consider a "personal loan" by their bank. Here again, if the business resides in a state where access to the UCC database is free, always search the database for filing information. If no filings exist, there are no loans outstanding which have a senior lien on accounts receivable.

**MANY ARE  
UNAWARE**

In many states, although you can search the UCC for filing information, you cannot view the image of the filing nor see the actual collateral subject to lien without paying a fee. If you cannot tell, just reference the loan and the filing on your submission. The factor will pull the record and find what collateral secures the loan.

- **TAX LIENS OR PAYROLL TAX ARREARAGES:** If a tax lien is present or tax payments are in arrears, find out the balance involved and also if a *payment plan* with the IRS is in effect. Tax liens are not necessarily deal breakers, but must be dealt with in a way that eliminates the ability of the IRS to levy the payments due from purchased customer accounts and *prime* the factor. Tax lien filings can also be searched in every state and usually for free.

**TAX LIEN  
PAYMENT PLAN  
INFORMATION**



EVEN IF THESE TWO (EXISTING LOANS AND LIENS) AREAS ARE LEFT UNCOMPLETED ON THE COMPANY PROFILE, YOU SHOULD ALWAYS SEARCH THE UCC FOR EXISTING LOAN FILINGS AND DO A TAX LIEN SEARCH IF POSSIBLE. The factor will quickly perform both once you submit the deal, but if you have access to free lien searches, its good policy to do both a UCC search and tax lien search.

## Common Submission Mistakes

As you should now know, deal submission in factoring is deceptively simple but there are several very common mistakes made by “newbie” brokers and they almost always involve identifying the type of financing needed. As a new freelancer, you will understandably be excited when you get your first completed company profiles, but don’t let your excitement allow you to make any of the following mistakes.

### AVOID SIMULTANEOUS SUBMISSIONS

- **SIMULTANEOUS SUBMISSION:** As an expert consultant, you always want to refer your clients to the right factor and get them a “good deal”. Never, however, fax or email simultaneous submissions to different factors at the same time. Simultaneous submissions are very much frowned upon in the industry and if discovered, will cause most factors to simply walk away from the deal.

Brokers should choose a factor carefully and then let that factor do its initial underwriting to either accept or decline the deal. The industry is very competitive from a fee standpoint and if you have chosen a factor in the right niche area and your client qualifies, there will be no need for any subsequent submissions.

### MOBILIZATION FUNDING

- **KNOW THE DIFFERENCE BETWEEN FACTORING AND CONTRACT FINANCE:** We've already discussed this in the previous chapter but here it comes again. The biggest mistake made by industry neophytes is the inability to know the difference between a financeable FACTORING deal and CONTRACT finance which involves no invoice but the need for what is termed *mobilization money* to get a project started.

Contract finance is similar to purchase order finance except for one major distinction:

- **Contract Finance** usually involves a small business who is the beneficiary of a contract to provide a service.
- **Purchase Order Finance** usually involves a small business who is the beneficiary of a purchase order to deliver goods.

Both involve the need for some form of mobilization funds, however contract finance involves additional risks that are unacceptable to almost all lenders since there is initially no collateral (no invoice or goods). See example below.

**Jim Smith owns a landscaping company and receives a \$30,000 contract to provide landscaping services for a local bank. The local bank has agreed to pay for the service in 30 days from completion.**

**To provide the service and fulfill the contract, Jim needs \$7,500 to purchase trees, shrubs, and to rent a backhoe. In other words, he needs *mobilization funds* to begin the work. He comes to Jonas, a local factoring broker he recently met at a Chamber of Commerce meetup for funding.**

**Jonas explains to him that what he needs is *mobilization funding*, not factoring. Once the job is completed and an invoice is then generated for \$30,000, it could easily be factored if required due to extended terms of payment given to the bank. But until the service is performed, there is no collateral in the form of a valid invoice for a lender to provide financing.**



## NOTES



Almost all "newbie" brokers make the mobilization funding mistake, usually because they think there might be something they're missing in the deal and it can somehow be done. So, they run it by a factor just to see. Mobilization funding deals will always be declined unless the funding is based on a valid invoice. Query the prospect to find out if he or she has other invoices where the work has been performed but payment has not been received. Perhaps these can be substituted and used to provide the needed funding.



## Deal Submission Step-by-Step

The following is a practical step-by-step guideline that will help you submit your first deal to a factor. It includes items you should review prior to submission.

- **COMPANY PROFILE:** Fax or email a company profile to your prospect and have them completely fill it out and sign it. Once completed, have them return it to you via fax or email. Make certain you have filled out the "Broker Info" on the profile so your factor is aware of who submitted this deal. (Company profiles in PDF format are available for download in the IACFB E-Learning Campus)
- **ACCOUNTS AGING REPORT / CUSTOMER LIST:** Your factor will want to review the names of the primary customers of the prospect for credit analysis. If possible, have your prospect send a customer list with addresses or/and an *accounts receivable aging report*. An A/R aging report shows all of the currently outstanding invoices of the business. If you do not provide this, the factor will request it from the prospect during underwriting anyway.
- **REVIEW THE COMPANY PROFILE:** Review the profile for completeness and take notice if the prospect listed any current loans or any tax liens outstanding. If these are present, call the prospect to get additional information. These are potential deal breakers and its best to get to the bottom of them early. If there is a...

### REVIEWING THE PROFILE

**Tax Lien Outstanding:** Find out the approximate dollar balance of the arrearage and if a payment plan is in effect. Factors must have a senior lien on accounts receivable to provide financing and an IRS lien subjects the accounts they purchase to possible levy.

**Prior Loan Outstanding:** If a prospective client has an existing business loan from a bank or similar lender, it is almost a certainty that lender has filed a lien and security interest upon the business assets. If possible, find out how the loan is secured (what is pledged for collateral) by accessing the UCC database.



- **LOCATE A FACTOR:** If the company profile is completed and there does not appear to be any "deal breakers" evident, locate a factor in your database that you feel is suitable to handle this type of transaction (i.e. industry or deal size). Contact the factor and ask to speak to someone in business development that can handle a "brokered" transaction. You will be connected to a principal of the firm or to a BDO (Business Development Officer).
- **INTRODUCE YOURSELF:** Introduce yourself and tell your contact that you have a deal you would like to submit. Ask if they would please email a *Broker's Agreement* for you to execute.
- **REVIEW THE BROKER'S AGREEMENT:** There are basically three (3) areas of primary importance on any standard factor's *Broker's Agreement*.

**Commission Rate:** this will usually be either 10%, 12.5% or 15% percent of the factoring fees earned but there are also some pretty "exotic" structures out there. Beware of broker agreements that pay based on "funds employed" as those pay based on the advance amount and may be less than a standard industry rate.

**10% - 15%  
COMMISSION RATE**

**Residual Life-of-Account Payment:** The vast majority of all factors pay for life of the account. A very few pay for only one year. Make certain the factor pays for account life.

**No Charge-Backs:** There should be no provision for charge-backs against the broker in the event the factor-client relationship fails.

If the *Brokers Agreement* is acceptable (and virtually 100% are), sign the agreement and return it to the factor or BDO. Always have a signed Broker's Agreement in hand before you send in the company profile. This tends to be a very honorable industry, but there are always exceptions.

**HAVE A SIGNED  
BROKER'S AGREEMENT  
IN HAND**

- **SEND IN YOUR DEAL & PAPERWORK:** Once you have a signed agreement, send in the company profile and other documents if you have any.



## NOTES

### INTRODUCE AND STEP OUT

- **CONFERENCE CALL:** On the cover page, ask about the BDO / factor's availability for a conference call with the prospective client. Work with the times provided and set up a conference call between yourself, the prospect and the factor. On the call, introduce the prospect to the factor or BDO. Then step out, listen, and learn.
- **DEAL FINALIZATION:** If the factor accepts the deal, you are done. The factor will close the deal, issue contracts, and begin the financing. There is nothing more for you, as the referrer, to do other than collect commission checks.
- **BACK TO WORK:** NOW...go find another five prospects!

## Initial Underwriting by the Factor

The initial underwriting by the factor will be accomplished very quickly, typically in just a few hours. After your submission and successful conference call, the factor will forward a *Terms and Conditions Agreement* (sample in the Learning Lab) to the prospect. This short, one or two page document outlines the provisions of the proposed factoring agreement.

If acceptable, the prospect will return the terms sheet with signature. The factor will then quickly perform a:



- **Corporate Records Search:** to validate the correctness of the business identity
- **Uniform Commercial Code Search:** checking for existing liens against accounts by an active lender
- **Tax Lien / Judgment Search:** to check for existing business or personal liens
- **Criminal Background Check** to investigate felony convictions for the owner or owners of the business

### VERY CREATIVE FINANCIERS

If any of the above four items are present, they are potential "deal breakers" if they cannot be addressed properly or rectified. Factors are very creative financiers, however, and in many instances such problems can be addressed satisfactorily.



# The Factoring Agreement

Once the client has signed the *Terms and Conditions* letter and a UCC and tax lien search concludes no liens exist, the contracting can be finalized with the client signing a standard factoring agreement (commonly called a *Master Purchase and Sales Agreement*). This agreement, among other things, will define and set forth the fee arrangement, authorize notification of assignment to customers, and define rules and guidelines for the factoring arrangement. It will also address events of default and their remedies.



**NOTES**

**STANDARD FACTORING  
AGREEMENT**

## Filing the UCC-1 Financing Statement

The *Master Purchase and Sales Agreement* authorizes the factor to file its UCC-1 Financing Statement, perfecting its security interest in the accounts receivable of the client. The UCC-1 is filed at the Secretary of State level in the state of the client's incorporation. Prior to making the first advance, the factor will normally conduct a second UCC search to make certain the filing is correct and senior in its lien position.

## Noticing the New Customers

As you know, *notification of assignment* provides the mechanism for a lender (factor) to take control of the invoice payments made by the customers of the new client. Once notified by the factor of its security interest in accounts receivable and the payments thereon, the client's customers are now obligated to pay the factor and no other entity. This means they will no longer pay the client.

**NOTIFICATION  
OF ASSIGNMENT**

Notifying the client's customers will usually be done two ways.

- **By Letter:** This will be a friendly but formal letter which addresses the assignment and the new "remit to" address of the factor or the factor's lockbox.
- **By Legend:** During the advance, a "notice of assignment" legend will be attached to the invoice. The factor may additionally have the client change the "remit to" address on the invoice template of its accounting software.



## NOTES

### Selective Notification

In some instances, a client may wish to factor only the invoices of a select group of customers and not all customers. For example, the client may have several large customers which take 30-45 days to pay their invoices, creating a cash flow hardship, and requiring factoring for a method of remedy. The client may also have some smaller customers who pay their bill in under 10 days. Factoring for such customers is simply not needed or required.

Such *selective notification* and financing is generally acceptable to most factors. The fact that certain customers are not being factored, however, does not affect the factor's security interest in all accounts. Should an event of default occur, the factor can quickly notify such "non-factored" account debtors and require them to begin making payments directly to the factor as well.

### Events of Default

The factoring agreement will define *events of default* which are those occurrences that can bring the factoring arrangement to an immediate and abrupt halt. Primary among those is something called *misdirected payments* or simply *collection*.

Obviously, when a factor purchases an invoice and notifies the customer regarding the assignment of the payment, the factor expects to be paid. *Collection* occurs when a client receives a misdirected payment from a customer on a purchased invoice in error, after valid notification of assignment has been made, and then does not immediately turn that payment over to the factor. *Collection* by a client represents civil theft and is justification for immediate termination of the factoring agreement...or worse!

**IMMEDIATE  
TERMINATION**

### Contract Term

The factoring agreement will define the contract term which will usually be one year. In most cases, the factoring agreement will automatically renew each year unless the factor is notified to the contrary by the client.

**AUTOMATICALLY  
RENEWS**

## The First Advance of Funds

When a the new client returns the signed contract, the factor will begin processing the first advance of funds. Most clients will have existing invoices already outstanding which can be included in this advance, provided they are less than 30 days old and the factor can achieve a valid notification prior to the invoices being paid. The client will add additional new invoices to its existing invoices and combined, they will be used to create the first advance of funds.

The factor will create something called an *advance schedule* which:

- **lists the purchased invoices consecutively by invoice number**
- **totals their amount**
- **multiplies the total by the factor's advance rate (typically 80%)**
- **reduces that total amount by any deductions (such as a wire transfer fee)**
- **determines the net advance amount to be wired to the client's business bank account.**



### NOTES

**INCLUDES  
OUTSTANDING  
INVOICES**

**CREATES THE  
ADVANCE SCHEDULE**

## The Verification Process

As you already know, factors are purchasing a piece of paper (an invoice) which is presented to them as valid by your client for goods delivered or services performed. Prior to an advance, factors will validate the invoices being purchased through *verification*.

## The Advance of Funds

When the factor's advance is finalized, it will be faxed, emailed or electronically made available to your client who will check the advance for accuracy and then sign the advance document. Once the advance is prepared by the factor and then signed by the client, the funds are disbursed within just a few hours through direct wire transfer to your client's business checking account.

**FUNDS  
ADVANCED**



## NOTES

### Processing Collections

With the invoices now purchased and customers noticed to make payment directly to the factor, payments will begin to be received. In some cases, payments will come directly to the factor's business address. But more likely, they will be received at a *lockbox*, which is a special post office box operated by a bank.

As payments are received, they are posted into the factor's invoice tracking software and a *collection report* is created. The collection report will provide all of the information regarding each invoice paid by the check, the customer's check number, the advance report number related of the invoice purchase, the advance date, the payment date, and the total fees earned by the factor.

## COMMISSION REPORTS

### Brokers Commission Reports

The commission report for the referring broker is based on the total collections received during the month for all referred clients. Most factors provide broker commissions monthly with the start date being the first of the month and the end date being the end of the month. The commission report itself is based on the sum of the various client collection reports generated during the period.



There are several standard formats used by factors for their broker reports but most will display both total purchases and total collections for the period. The *collections* will show the factor's fees earned and then multiply that amount by the broker commission rate. The *purchases* made during the month will provide the broker with a snapshot of what fees will be earned in the near future.

The client does not see the referring broker's monthly commission report. It is also important to note that the factoring fee rates charged to a client are not affected by the fact it was referred by a broker. Brokers are simply looked at as an internal sales expense and cost of doing business, the same as if the client was generated by one of the factor's in-house BDOs.

# Factoring Broker Commissions



OK! Now for the good part...the MONEY! Freelance brokering is a very, very lucrative occupation and the commissions and referral fees paid are extraordinary. And, there are many types of commissions depending on the financial product. Here, however, we will focus strictly on those associated with factoring.

Commissions paid to independent factoring brokers tend to be relatively unique in the commercial finance industry. This is because they are:

- **RESIDUAL:** This means they are paid on a continuing recurring basis each month based on collections
- **LIFE-OF-ACCOUNT:** This means you will receive such residual commission payments for as long as your referral continues to use the factor's services

## LIFE-OF-ACCOUNT COMMISSIONS

This commission style is also common for purchase order finance referrals but most other product areas pay a one-time fee in "points" (a percentage of the loan amount) much like a typical real estate loan.

Referral commission fees paid to brokers are most often 10%-15% of the fees earned by the factor. This range depends on the factor, the size of the account, the factoring arrangement's fee structure, and the amount of continuous business you, as a broker, send to a particular factor. Factors will also run periodic bonus programs or sales contests where commissions can occasionally be a slightly higher percentage of the factoring fees earned.

## FACTOR'S BONUS PROGRAMS

Broker commissions are paid monthly and you will usually receive a check during the first week of the calendar month for commissions generated the previous month. When first submitting a deal for financing, it will often take two (2) months or more before you receive your first full commission check. This is because your fees are based on the factoring fees which, in turn, are a function of collections. Factors must purchase and then be paid on invoices before service fees can be tallied and broker commissions paid.



## TAKE THE QUIZ

### Chapter 4 Quiz

1. A "generic" application used by many new industry brokers is called a\_\_\_\_\_
  - A. company profile
  - B. client profile
  - C. financing application
  - D. none of the above
2. Brokers can download generic company profile forms at\_\_\_\_\_
  - A. the IACFB Annex
  - B. The Learning Lab
  - C. Campus IACFB
  - D. all of the above
3. When a client completes an application as a corporation or a LLC, a search of the Secretary of State's corporate records should show an \_\_\_\_\_ status.
  - A. filed
  - B. revoked
  - C. active
  - D. franchised
4. A lien on a security filing which takes "all assets" of a business as collateral is referred to as a \_\_\_\_\_
  - A. Total lien
  - B. Blanket lien
  - C. Full security lien
  - D. Full Recourse lien
5. Simultaneous submissions are considered normal when submitting deals.
  - A. True
  - B. False

6. One of the biggest mistakes all new brokers make when submitting their first deals is knowing the difference between purchase order finance and \_\_\_\_\_
- A. factoring
  - B. floating lien finance
  - C. contract finance
  - D. all of the above
7. If possible when submitting a deal, include a (an) \_\_\_\_\_
- A. IRS lien report
  - B. collections report
  - C. accounts receivable aging report
  - D. all of the above
8. The normal commission rate for factoring submissions is \_\_\_\_\_
- A. 5-10 percent
  - B. 10-15 percent
  - C. 15-20 percent
  - D. 20-25 percent
9. On factoring submissions, brokers receive commissions that are \_\_\_\_\_
- A. life-of-account
  - B. residual
  - C. paid in points
  - D. both A and B above
10. The client factoring agreement is also called the \_\_\_\_\_
- A. Discount and Advance Agreement
  - B. Sales Advance Agreement
  - C. Master Purchase and Sales Agreement
  - D. None of the Above



**TAKE THE QUIZ**

**ANSWERS TO  
THESE AND OTHER  
QUESTIONS CAN  
BE FOUND IN THE  
BACK OF THE GUIDE**

