

Accounts Receivable FACTORING



BOAT TRAILER CO.

Boat Trailer Co. is a small builder of boat trailers and related products such as trailer frames and axles in Southwest Florida. Bill James, it's owner, was awarded a contract to supply the *Florida Fish and Wildlife Conservation Commission* with 72 new trailers to replace old units that were rusty and failing. Each trailer was \$2,900 for a total value of \$208,800.

Bill had 20 trailers in inventory to begin delivery and the purchase order called for all trailers to be

delivered within 60 days of the contract being awarded.

Boat Trailer Co. had little excess capital. The problem it would now face is that the state pays slowly and Bill knew he would not receive payment for the 20 trailers he could immediately deliver for nearly 45 days... cash he needed to order bulk steel and hardware to build the remaining 52 trailers and to be able to deliver them by the 60 day mandated purchase order deadline.



The Problem: Raw Materials / Inventory

Bill James had virtually no credit history but decided to go to his local community bank anyway, explain his problem, and request a short term loan. The loan officer explained that what James really needed was *factoring*, a method of financing his accounts receivable that did not require a strong credit history for him, only his customers. And, as luck would have it, the community bank had a *factoring* department and James was introduced to the bank's *factoring* officer, where an account was immediately established to provide the necessary working capital to meet the order.

Through *factoring*, James would receive an initial advance from the bank of \$46,500 (80%) on the

\$58,000 invoice after delivery of the 20 finished trailers in inventory. That advance of \$46,500 was enough to then buy the bulk steel and hardware to complete the other 52 trailers in time to meet the required delivery deadline. After the state paid for the 20 trailer shipment, the bank would then give James the \$11,500 not initially advanced, less a small factoring fee the bank charged for it's services.

Even more important, with the bank's *factoring* arrangement now in place, James could begin to bid on many more state and municipal contracts, jobs he had shunned in the past due to the slow payment policies of those entities. The *factoring* arrangement was exactly what James needed to take his small

company to the next level. It sped up the company's cash flow so much that James was able to pay his steel and parts suppliers within 10 days of delivery and take a 2% discount for early payment. That discount for materials offset nearly 75% of the bank's *factoring* fee, making the overall expense for the *factoring* facility minuscule.

Another surprise to James was that the *factoring* arrangement with the bank had no upper credit limit.

So long as James sold to approved, creditworthy customers, the bank would immediately advance on each invoice once the trailers were delivered. There were no requirements for lengthy lending committee meetings to approve any credit line increase. So long as the invoices were bonafide and legitimate, the cash was available. The only limit to the growth of **Boat Trailer Co.** was now how many large contracts Bill James could acquire.

Factoring for Inventory and Raw Materials

While *factoring* is strictly a method of financing the terms of payment granted to customers on accounts receivable, there is obviously no limitation on what the *factoring* advances of cash can be used for.

Many small manufacturers will use the proceeds from invoice *factoring* to supplement their current working capital to purchase inventory, raw materials, and even equipment for a pending job. In instances

where large contracts require the temporary rental of expensive, heavy equipment, the injection of working capital from *factoring* the outstanding invoices on finished work often fills the bill and provides the necessary working capital required on current projects.

Factoring

The World's Most Popular Method of B2B Small Business Finance

