



A DIVISION OF SCALE BANK



BROKER GUIDE

Invoice Factoring

Helping Brokers Navigate Factoring Confidently and
Create Long-Term Client Value

www.getscalefunding.com

Table of Contents

Introduction to Factoring	2
Why Companies Use Factoring	2
Understanding Factoring Fundamentals	3
The Factoring Process	3
Types of Factoring.....	4
Benefits of Factoring for Clients	4
The Broker's Role in Factoring	5
What Brokers Need to Know	6
Identifying Suitable Clients	6
Working Effectively with Factoring Companies	6
Potential Challenges and How to Address Them	7
Real World Scenarios	7
Frequently Asked Questions	8
Conclusion	9

Introduction to Factoring

Factoring is a financial transaction that allows businesses to unlock the cash tied up in their accounts receivable. Instead of waiting 30, 60, or 90 days to get paid by their customers, companies can sell their invoices to a factoring company (or "factor") for immediate working capital. Unlike a loan, factoring is not debt; it is the sale of an asset, the invoice. This distinction is important for businesses that want to avoid additional liabilities on their balance sheet or don't qualify for traditional bank lines of credit.

Factoring is especially common in industries with long payment cycles and ongoing working capital needs, including:

- Transportation and logistics
- Temporary Staffing
- Oilfield and energy services
- Manufacturing and fabrication
- Mechanical and building-related services

This guide is designed to help brokers confidently discuss factoring, identify promising opportunities, and avoid common pitfalls. The goal is simple: enable your clients to access cash without incurring debt and cultivate enduring referral partnerships in the process.

Why Companies Use Factoring

Factoring provides fast access to cash without the hurdles of bank financing. Businesses use it to:

- Make payroll and cover operating expenses.
- Buy materials, fuel, or inventory.
- Invest in new projects or equipment.
- Stabilize cash flow during periods of growth or customer delays.

Understanding Factoring Fundamentals

To effectively guide your clients, it's crucial to have a firm grasp of factoring's core concepts and terminology.

- **Accounts Receivable (A/R):** These are the outstanding invoices that a business has issued to its customers for goods delivered or services rendered, representing money owed to the business.
- **Debtor:** The client's customer who owes the invoice amount.
- **Factor:** A factoring company that purchases a business's accounts receivable.
- **Advance Rate:** The percentage of the invoice value that the factor advances to the business. This is typically 70% to 90%, with the remainder held as a reserve.
- **Reserve:** The portion of the invoice value that the factor holds back until the customer pays the invoice, from which the discount fee is deducted.
- **Discount Fee or Factoring Fee:** The fee charged by the factor for its services, calculated as a percentage of the invoice value. This fee varies depending on the volume, the creditworthiness of the client's customers, and the length of the payment cycle.

The Factoring Process

The factoring process generally involves these steps:

1. **Client Provides Invoices:** The business (client) provides the factor with its invoices to customers (debtors).
2. **Factor Verifies Invoices:** The factor verifies the validity of the invoices with the client's customers.
3. **Factor Advances Funds:** The factor advances a percentage of the invoice value (the advance rate) to the client.
4. **Customer Pays Factor:** The client's customer pays the invoice amount directly to the factor.
5. **Factor Releases Reserve:** The factor releases the remaining reserve to the client, minus the discount fee.

Types of Factoring

Brokers should be familiar with the two primary types of factoring:

- **Recourse Factoring:** In recourse factoring, the client is liable to repay the factor if the debtor does not pay the invoice. The factor has "recourse" back to the client.
- **Non-Recourse Factoring:** In non-recourse factoring, the factor assumes the risk of non-payment by the debtor (with some exceptions, such as disputes). Non-recourse factoring is typically more expensive due to the increased risk for the factor and is often limited to instances of debtor failures.

Other variations include:

- **Spot Factoring:** Factoring individual invoices on an as-needed basis, rather than an ongoing arrangement.
- **Full-Service Factoring:** In addition to advancing funds, the factor may also handle customer credit checks, collections, and accounts receivable management.

Benefits of Factoring for Clients

Factoring offers several compelling benefits for businesses:

- **Improved Cash Flow:** The most significant advantage is immediate access to working capital, which helps businesses meet operational expenses, invest in growth, and take advantage of opportunities.
- **No Debt Incurred:** Factoring is not a loan, so it does not create debt on the balance sheet, preserving borrowing capacity.
- **Faster Access to Funds:** Factoring can provide quicker access to cash than traditional loans, which often involve lengthy application and approval processes.
- **Potential Credit Improvement:** By improving cash flow and enabling timely payments to suppliers, factoring can indirectly enhance a business's creditworthiness and, over time, make a business more "bankable."
- **Back-Office Efficiencies:** Some factoring services include accounts receivable management and collections, freeing up the business to focus on its core operations.
- **Broader Eligibility:** Because factors rely primarily on the creditworthiness of debtors, businesses with little or even poor credit history may qualify.

The Broker's Role in Factoring

Brokers play a vital role in connecting businesses with suitable factoring solutions. Here's a breakdown of the broker's key responsibilities:

1. Lead Generation and Qualification:

- a. Identify potential clients through networking, referrals, online marketing, and industry events.
- b. Qualify leads by assessing their business needs, financial stability, and suitability for factoring.

2. Client Needs Assessment:

- a. Understand the client's specific cash flow challenges, industry, customer base, and invoice volume.
- b. Determine the most appropriate type of factoring.

3. Matching Clients with Factors:

- a. Leverage your network of factoring companies to find those that specialize in the client's industry and offer the desired services.
- b. Consider variables such as underwriting requirements, advance rates, fees, contract terms, and customer service reputation.
- c. Identify reputable factoring companies that can act quickly and professionally.

4. Negotiating Terms:

- a. Advocate for your client to secure favorable terms, including competitive advance rates and discount fees.
- b. Ensure that the client fully understands the terms and conditions of the factoring agreement.

5. Closing the Deal:

- a. Facilitate the smooth execution of the factoring agreement.
- b. Help the client identify and gather any documents needed for underwriting.
- c. Maintain communication between the client and the factor throughout the process.

6. Broker Compensation:

- a. Brokers typically earn a commission, usually a percentage of the factor's fees, for each successful deal.
- b. Commission structures can vary, so it's essential to clarify them with the factoring company upfront and in writing.

What Brokers Need to Know

Not every client is a good fit for factoring. As a broker, you should look for:

- Businesses with commercial customers (B2B, not B2C)
- Invoices for completed verifiable work.
- Customers with reasonable credit profiles.

Red flags include:

- Customer concentration (one customer is more than 50% of revenue)
- Poor invoicing habits or disputed charges
- Existing or recent lender conflicts, tax liens or UCC filings

Understanding the structure of a factoring deal, advance rate, reserve, and fees, helps you explain it clearly and set realistic expectations.

Identifying Suitable Clients

Factoring is particularly well-suited for businesses that:

- Have consistent sales with repeat customers but experience slow customer payments at the same time they have cash needs.
- Are experiencing rapid growth and need working capital to support expansion.
- Have difficulty obtaining traditional bank financing due to credit history or other reasons.
- Operate in industries with long payment cycles (as mentioned earlier).
- Need to improve their cash flow to meet payroll, pay suppliers, or invest in inventory.

Working Effectively with Factoring Companies

Building strong relationships with factoring companies is crucial for broker success:

- **Research and Due Diligence:** Thoroughly research potential factoring partners. Evaluate their experience, reputation, financial stability, and industry specialization.
- **Understand Factor Requirements:** Familiarize yourself with each factor's underwriting criteria, documentation requirements, and approval process.
- **Clear Communication:** Maintain open and transparent communication with factors throughout the deal process.
- **Provide Accurate Information:** Ensure that all information provided to the factor is accurate and complete.

- **Negotiate Fair Terms:** Advocate for your client while also being mindful of the factor's needs and profitability.
- **Build Long-Term Relationships:** Cultivate long-term partnerships with factors based on trust and mutual respect.

Potential Challenges and How to Address Them

Brokers should be prepared to address potential client concerns about factoring:

- **Cost:** Factoring is generally more expensive than traditional bank loans. Emphasize the benefits of improved cash flow and avoiding debt.
- **Control:** Some clients may be concerned about relinquishing control over collections. Explain the factor's professional approach and focus on maintaining positive customer relationships.
- **Due Diligence:** The factoring process involves due diligence, which some clients may find intrusive. Reassure them that this is a standard practice to verify invoices and minimize risk.

Real World Scenarios

- **Scenario A: Transportation Company**
A growing trucking company hauls freight for large brokers and shippers with 30 to 45 day payment terms. The company needs to pay for fuel, insurance, and drivers weekly. Factoring provides consistent cash flow, allowing them to take on more loads without waiting to get paid.
- **Scenario B: Staffing Agency**
A staffing firm provides skilled labor to industrial clients and has to pay weekly payroll. Their customers pay in 45-60 days. Factoring ensures payroll is covered even when new contracts ramp up quickly.
- **Scenario C: Service Company**
An industrial welding company lands a big new contract. They need funds to buy new equipment and hire employees, but they won't be paid for several months. Factoring allows the company to take on the project, knowing they'll have cash flow as soon as their first invoice.

Frequently Asked Questions

Is factoring a loan?

No. It's the sale of an asset (an invoice). There is no debt added to the balance sheet.

Will my client's customers be notified?

Yes. Factors send a Notice of Assignment, but reputable ones handle this professionally.

How fast is funding?

Initial setup takes 3-5 days. After that, advances are typically within 24 hours.

What happens if the customer doesn't pay?

In recourse factoring, the client must repay the advance. In non-recourse, the factor assumes some credit risk depending on the structure.

Is factoring only for distressed businesses?

No. Many growing companies use factoring to avoid stretching cash during expansion or the time and expense of managing accounts receivable.

Red Tape: Contracts & Restrictions

Before referring a client, confirm its customer contracts don't prohibit invoice assignment. Look for phrases like:

- "No assignment without written consent"
- "Proceeds may not be pledged or factored."

Factoring companies typically perform a UCC search and review these agreements. But catching it early saves time and avoids deal-killers. While it is illegal for any company to not "allow" a vendor to factor, it may be a risk to the relationship to proceed with it.

Conclusion

Factoring provides a valuable financial solution for businesses seeking to improve cash flow and fuel growth. By understanding the fundamentals of factoring and mastering the broker's role, you can effectively serve your clients, build strong partnerships, and establish a thriving brokerage business.

Scale Funding has a proven track record of partnering with brokers to facilitate successful factoring deals, providing reliable funding solutions and excellent service.

Scale Funding has partnered with brokers nationwide to deliver reliable factoring solutions and outstanding service. Contact us today for a consultation or visit <https://getscalefunding.com/industries/broker-referral/> to join our broker program.

(800) 707-4845

info@getscalefunding.com

www.getscalefunding.com

7600 Parklawn Avenue | Edina, MN | 55435