Money is the lifeblood of any business. This issue explores alternative ideas to manage, grow and uncover revenue that many new and small business owners may not be aware of. New Business Minnesota presents these experts to help show you the way: Pam Krank, The Credit Department Inc. on Credit Management; Lesley Farmer, KLC Financial Inc. on Equipment Leasing Alternatives; and Rochelle Hilson and Kristin Erickson, North Mill Capital on Factoring Invoices.
As your business grows, there will be times when you need capital to build inventory, buy equipment or pay your suppliers. And you may find that a willing bank is not to be found.

At moments like that you need to know your financing options. One solution that many new and growing business owners should know about is called factoring.

Factoring is a financing tool based on the purchase of accounts receivable – invoices. It is essentially the same as a loan. Here is how it works.

• Factoring companies like us, North Mill Capital (NMC), will buy the receivables at a mutually agreed upon advance rate.
• NMC lends up to 85 percent of the receivables value upfront.
• When the invoice is paid by our client’s customer, NMC gets paid for what was already loaned out. The balance is then returned to our client, less our fee.

North Mill Capital’s role is to provide a funding source to bridge the period of time until the business can obtain bank financing. And because we aren’t regulated, we can provide the borrower with flexibility that a bank can’t. Often, our clients choose to stay with us when they could otherwise leave.

Lenders, like banks, look for cash flow and profits to guide their decisions. They analyze the historic performance of the borrower to determine if they can lend money today. In other words, if you are a new business with only limited history or you launch a new service or product that has yet to establish a track record, you may not fit the bank’s lending criteria.

Our approach is different. NMC looks at the collateral already in place, such as receivables, inventory and equipment. Then we evaluate our client’s prospective outlook and determine how comfortable we are with future performance.

New businesses or those that are growing faster than their cash flow and bank can accommodate are the most in need of factoring services.

Borrowing through a factoring relationship ensures that the debt remains within a healthy balance with assets so it is hard to overburden a company.

NMC often works with banks where we share the financing.
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arrangement. The client can continue with factoring or return to full bank financing whenever the bank and the client are ready. It can be a short-term or long-term relationship.

Factoring services are a good alternative in either a strong or a weak economy. Companies who might otherwise be unable to obtain sufficient bank credit can rely on factoring as an alternative during that time frame.

Factoring has been around for centuries, and is a great financing tool regardless of the market.

Case Study

We have a client who manufactures high-end planters for fruits and vegetables. Their growth rate was rapid, and further complicated due to the seasonality of their business. Our factoring solution provided them with more than sufficient credit availability.

We also provided a short-term inventory loan so they could get through their season and deliver to their large retail customers without creating a lot of debt.

Just as important, they didn't have to raise equity – sell off part of the business to investors. They got their money and continued to own 100 percent of their business.

Industries typically utilizing factoring include manufacturing companies, service providers (staffing companies, security guard services, etc.) and wholesale distributors.

Some borrowers are in a start-up phase and some have been in business for more than 50 years.

Most clients are referred to us by a bank, accountant or lawyer who recognize an alternative source of funding is needed. The borrower often doesn’t know anything about factoring, just that they have a need for operating capital.

Factoring Misconceptions

While some businesses turn to factoring because they are experiencing financial challenges, more businesses turn to it because they are experiencing significant growth.

Another misconception about factoring is that the client’s customers have to pay the factor directly. NMC operates seamlessly with our clients and their customers are not usually aware of the financing arrangement.

Some business owners mistakenly assume that factoring is too expensive. It is more expensive than borrowing from a bank, but it’s less expensive than equity. Factoring is often a short-term tool that is used until you can build a track record that will qualify for a bank line of credit.

Online Lending

If you have a financing need, there is a good chance you’ll turn to Google, where you’ll find all kinds of options that appear to solve your problem. The latest financing trend is peer-to-peer or fintech (financial technology) financing online.

It may be a quick and easy source of money, but they have no real knowledge about you or your business and there is no personal relationship. Your information is plugged into a credit scoring model and you qualify or you don’t. It can be difficult to understand their pricing and it can be prohibitively expensive.

You are much better off working with a local lender that can help you work on a comprehensive solution. NMC has a full-service office that has an extraordinary amount of experience and significant capital resources.

We believe being local is a big plus for our clients. NMC wants to be a lending partner with a relationship manager who knows and understands our client's business.

Building that relationship begins at the first meeting with a prospective borrower where we learn about our prospect’s business and financial needs to see if it’s a good fit. We then evaluate the financial statements and aging reports for receivables and payables. If it makes sense for us and the borrower, we prepare a proposal.

How much we are offering to lend is explained in detail in the proposal. If it is accepted, we move on to due diligence and underwriting and then close the transaction.

It can all come together as quickly as a week, or it can take much longer depending on a number of factors. The better prepared the client is, the faster it goes.

If a client has a need that is outside our parameters, we might be able to work around that or we can refer them to the right solution. We think it’s important to surround yourself with successful professionals like good banking and accounting partners. Our clients see us in that mix.

We can also help our client’s manage their accounts receivable process, monitor their customer’s credit on an ongoing basis, make collection calls if needed and generally help manage their receivables portfolio.

Conclusion

We can’t stress enough how important a good business relationship is. A client may come to us at first thinking they just need financing, but as we work with them, they realize NMC can help them in other parts of their business.

What makes this business fun for us is seeing a company that is struggling to get credit, and we are the ones who can make it work. Our success stories are extremely gratifying.

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Call To Action

To learn more about factoring and see if it is right for your company, call Kristin at (952) 259-6222.