

DEBT FACTORING – AN ALTERNATIVE TO FINANCE

Debt factoring firms have experienced an increase in demand as business seeks to settle outstanding accounts to boost cash flow. The demand has also increased as a result of diminishing access to credit.

The Benefits

Factoring and invoice discounting can allow businesses to circumvent cash flow difficulties by providing services which can either take over the administration of the trade receivables including debt collection functions while also provide funds against outstanding invoices.

This allows a business to maximise the use of its most valuable asset, an unpaid invoice. It may also provide a more commercially viable alternative to the administration costs and time involved in chasing outstanding invoices.

What is factoring and discounting?

Factoring and discounting is also known as cash flow or debtor finance.

Invoice discounting involves a business converting its unpaid invoices into cash by selling them to a debt factoring firm.

In the case of discounting the business retains the responsibility for collecting the debt with the benefit of the debtor not being aware of any involvement by the discounter.

In the case of factoring the debt is purchased by the factor and the factor carries out some part of the accounting function as agreed with the business. The debtors are aware that the debts have been assigned to the factor and that payment must be made to the factor to discharge the debt.

How do you become eligible?

As the demand for debt factoring services increase, so does their risk and eligibility criteria. Factoring and discounting require:

- A certain annual turnover;
- Goods sold on normal credit terms;

- A spread of debtors so that no one debtor is responsible for a large part of the total outstanding debt;
- Business customers who have an efficient debtor ledger and credit assessment system;

Factoring services are more suited to a business that:

- has rapid sales growth;
- has sales in tangible goods and services;
- has profitable trading and can demonstrate emerging profitability;
- regularly exceeds its current overdraft limit;
- is unable to meet large orders or seasonal peaks;
- is fully borrowed against fixed assets;
- has credit terms with trade debtors;
- has a suitable credit history;
- has most sales not on consignment or "sale or return".

Summary

The Government has recently proposed changes to personal property security legislation which will include to streamline factoring and discounting service providers. This should have the benefit of providing a greater confidence to fixed and floating charge holders. It is still unclear as to the impact of these proposed changes combined with the tighter regulation provided by the anti money laundering legislation.

In order to maximise your eligibility to this ever increasing alternative to cash flow and finance, lawyers can advise and assist with your risk management issues and debt recovery procedures.

If you would like any further information on this topic, please contact Irena Reiss on 8239 6505 or irena.reiss@kreissonlegal.com.au

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