

# Doron F. Eghbali Business Law

## What is Factoring and How Should Businesses Use It for Cash Flow?

Monday, July 12, 2010 by [Doron F. Eghbali](#)

Many businesses worry about whether their customers pay them or whether their customers pay them on time so that they can manage their cash flow liabilities. You might have heard of "factors" who provide specialized assistance to businesses in securing accounts receivables. However, factoring is not for every business and businesses should exercise caution and prudence in utilizing services of such companies.

### WHAT IS FACTORING?

Factoring is referred to companies specialized in securing businesses account receivables in exchange for several percentage points for servicing fee. In fact, the factor advances most of the invoice amount usually between 70-90% after checking out the credit worthiness of the billed customer. When the customer pays, the factor forwards the money to business while keeping a percentage of the transaction as "factoring fee".

### WHAT ARE SOME OF THE ADVANTAGES AND DISADVANTAGES OF FACTORING?

#### 1. ADVANTAGES

- **Relatively Easier for Start Ups to Qualify:** Factors unlike banks look mostly at the credit worthiness of customers not the credit worthiness of businesses. This makes it possible for start up companies with relatively little or no credit history to take advantage of this service.
- **Relatively Immediate Access to Accounts Receivable:** Businesses taking advantage of factors will have access to cash within 24-48 hours after sending an invoice to a factoring firm.
- **Relatively Easier Access To Foreign Markets:** Since factors shoulder the liabilities associated with accounts receivable, it make sense for businesses aspiring to expand overseas to use factoring services. Despite the high costs, it might facilitate such overseas expansion, if such expansion is predicated upon sound business plans.

## 2. DISADVANTAGES

- **Factoring is Costly for Many Businesses:** In fact, factors charge relatively more than traditional lenders for their services. This means factors charge often SEVERAL percentage points more than conventional lenders.
- **Factoring is Not Suitable for Relatively Small Businesses:** Since factors charge for every invoice high percentage points in factoring fees, it is imprudent and very costly for small businesses with relatively small-denomination invoices.

---

**DORON EGHBALI** is a Partner at the Beverly Hills Offices of Law Advocate Group, LLP. He Primarily Practices Business, Real Estate and Entertainment Law. Doron Can be Reached at: 310-651-3065. For More Information, Please, Visit

[www.LawAdvocategroup.com](http://www.LawAdvocategroup.com).