capitalise®

FINANCING INVOICES

Invoice Finance cheat sheets for accountants

For firms operating in the business to business marketplace Invoice Finance (IF) can be a vital product to ensure sufficient working capital for both day to day costs, as well as growth or acquisition ambitions. It can also be important to ensure overtrading doesn't occur, after all cash is king!

IF, at present, is fundamental in order for businesses to 'regrow' revenue back to pre-covid levels and beyond. A misunderstood product in the market, IF is used by some of the most well known and successful businesses in the UK.

Typically IF is seen in the following sectors:

- Recruitment
- Wholesalers
- Manufacturing
- Engineering
- Construction - specialist construction IF applies
- Transport

READ THROUGH BITE-SIZE CHUNKS ON:

1. What is Invoice Finance
2. Invoice Factoring
3. Invoice Discounting
4. Selective Invoice Discounting/Spot Factoring
5. Pros and Cons
6. Invoice Finance - CBILS lenders

What is Invoice Finance?

Invoice Finance is one of the most powerful B2B funding products available in the market. With approximately £80bn of cash flow provision annually, it powers cash up flow intensive businesses across the entire country. However, looking closely at the number of SMEs using IF in the UK, approximately only 40,000 businesses are benefiting from this product.

When used well, it is a very cost effective way to leverage business assets to provide funding.

Invoice Finance, as a product, is simply when a business 'sells' an invoice to a finance provider. This can be a single invoice or the full debtor book. The finance provider will pay the business up to 90% of the value of that invoice upfront, with the remainder being paid as per normal trading terms minus lender fees.

Invoice Factoring

Invoice Factoring is a whole ledger Invoice Finance product, which will typically run on a 12 to 24 month contract.

CREDIT CONTROL

With invoice factoring the credit-control responsibility is now with the finance provider. The finance provider will assume control of ensuring invoices are paid by the debtor.

PRICING

- Discount charge: 1-5% of the funds drawn on the facility
- Service fee: 0.10-2% of the turnover through the facility
- Arrangement/renewal fee: 0.25-1.5% of the facility each year

TYPICAL ADVANCE RATES

Between 60-90% of the debtor book depending on the size and credit worthiness of the debtor.

TIMESCALES

- 1-3 months
- As debentures need to be put in place along with verifying the book debt, it is important to allow enough time before the funds are needed
- If a client is refinancing a facility you must consider their notice period which can often be between 30 days - 3 months

SECURITY

Typical security requirements:

- A first ranking debenture over the business
- Personal guarantees from directors/ shareholders are often required

ADDITIONAL FACTORS

- Simple and easy to use
- No concentration restrictions
- No requirement for reconciliations
- Hand over credit control which can save time and money
- More expensive than Invoice Discounting

Invoice Discounting

Invoice Discounting is a whole ledger Invoice Finance product, which will typically run on a 12 to 24 month contract.

CREDIT CONTROL

With Invoice Discounting the business continues to be responsible for credit control, ensuring invoices are paid on time.

PRICING

- Discount charge :1-4% of the funds drawn on the facility
- Service fee: 0.10-1.5% of the turnover through the facility
- Arrangement/renewal fee: 0.25-1% of the facility each year

TYPICAL ADVANCE RATES

60-90% of the debtor book

TIMESACLES

- 1-3 months
- As debentures need to be put in place along with verifying the book debt, it is important to allow enough time before the funds are needed
- If a client is refinancing a facility you must consider their notice period which can often be between 30 days - 3 months

SECURITY

Typical security requirements:

- A first ranking debenture over the business
- Personal guarantees from directors/ shareholders are often required

ADDITIONAL FACTORS TO CONSIDERED

- Can be confidential
- Cheaper in comparison to Invoice Factoring
- Maintain credit control
- Month-end reconciliations require time and work
- Concentrations restrictions can apply

Selective Invoice Finance or Spot Factoring

Selective Invoice Discounting or spot factoring is where individual invoices (or receivables) are sold to a lender at a discount to raise funds.

CREDIT CONTROL

Client will maintain responsibility for credit control if they discount the invoice, and if they factor it, the lender will assume control of ensuring the invoice is paid.

ADVANCE RATES

50-90% face value of the invoice

SECURITY

Selective Invoice Discounting can range from being completely unsecured, backed by a personal guarantee, or the lender may take a debenture.

PRICING

- 1-5% face value of the invoice
- Interest accrued while funds are outstanding

TIMESCALES

1 week - 1 month

ADDITIONAL FACTORS

- Very useful for businesses who have one or two debtors on 60+ payment terms
- Can be expensive if used for large parts of the debtor book - it is always more expensive on a per invoice basis than ID or IF
- Drawdown rates can be lower at 50-70% depending on the creditworthiness of the debtor

Pros and Cons

PROS OF INVOICE FINANCE LENDING:

- Fully flexible to suit the business requirements
- Often able to obtain far greater credit lines as you are leveraging the assets within the business
- No tangible security required (which would be for sizeable overdrafts)
- Sometimes no or limited personal guarantee needed
- Debtor protection can be added for a fee
- By transferring the responsibility of credit control to the lender it can free up valuable time and money (invoice factoring)
- Debtors, as proven, are more likely to pay on time when lenders control ledgers or chase invoices
- New facilities can be drawn in a week to 10 days

CONS OF INVOICE FINANCE LENDING:

- Can take months to put in place for complex structures (overseas or Trade Finance)
- Often (incorrectly) associated with failing businesses
- Can be more expensive than an overdraft or revolving credit facility when looked at on a pure cost basis (not taking into account potential time/cost savings). However, facilities of a similar size to IF are often secured against personal property
- Can be additional costs such as CHAPS for same day drawdown as well as re-factoring fee
- Can be debtor concentration restrictions
- Not suitable for those business with short debtor days

CBILS - Invoice Finance

For a business requiring extra working capital, or that has been looking into IF, now is the perfect time to use it. There is a completely free market offering in place (first 12 months) across both selective IF and full debtor book IF.

Under the CBIL framework, the service fees and discount fees are paid by the Government for any invoices that matures within the 12 month period on any facility arranged prior to the conclusion of CBIL support.

MarketFinance - Selective Invoice Finance

- Facilities from £50k to £5m
- No fixed contract
- 6 months trading history (1 year construction)
- Service fee of 0.5-3.49%
- Discount fee of 0.5-1.5% per 30 days
- Advance rates of 55-90%

GapCap - Invoice Finance

- Facilities from £100k to £3m on full debtor ledger (some flexibility)
- Contract length 2-3 years
- Service fee of 0.5-1.0%
- Discount fee of 4-8%
- 1st ranking Debenture will be required
- Advance rates of 70-90%