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To stay afloat, firms turn to new financing

by Claude Solnik

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A Long Island firm with a $150,000 line of credit had a chance to make some easy money by buying and reselling merchandise. But the company also had a problem: It would cost $500,000 – more than three times its credit line – to make the deal. Since the firm lost money in the prior year, had a negative net worth and bills past due more than 90 days, it wasn't an ideal candidate for a loan or larger credit line.

The company, which was buying merchandise to sell to a big-box retailer, went to a factor who loaned money based on the receivables the deal generated. The factor decided the big-box retailer was a good risk, even if the firm itself might not be. The factor loaned the money in return for the right to collect directly from the store.

"They're selling to a healthy, large retailer," said Neil Seiden, managing director of Port Washington-based Asset Enhancement Solutions, which arranged the financing. "The factor is making a risk assessment based on the customer. That's what they do with factoring, look at the viability of the customer."

While traditional loans typically offer the best interest rates, a crackdown on credit, tightening standards and a tough economy are breathing new life into alternative financing and factoring – or the selling of receivables – in particular.

James L. DiCamillo, executive vice president of financial services firm Resource Management Partners in Islandia, said, "During these difficult financial times many companies are looking to alternate funding sources," such as factoring.

Delays in payment as customers hold onto cash make selling receivables more attractive – since firms otherwise may have to wait months to collect. And deteriorating economic conditions make it tougher for firms to get credit lines.

"Factors see it as a big opportunity to lend to small businesses, because the banks are tightening down. Some banks are pulling lines," said David Alibrandi, chief executive of Alliance One, a factor based in Hauppauge. "It gives you the cash when you need it."

Seiden said, "Asset-based lending is becoming more popular," since it relies more on the health of a particular invoice than of the borrower, which may be facing tough times. And firms are overcoming their own fears of factoring.

In the past, Seiden said, companies often were reluctant to seek nontraditional, short-term, asset-based loans, such as factoring, due to high costs and stigma. But this type of borrowing is becoming a lifeline when other loans aren't available.

"It used to have a negative connotation," Seiden said. "It doesn't really have that connotation so much anymore."

On the down side, major factors such as CIT cut back after taking losses due to mortgage backed securities. And factoring and other forms of asset-based lending cost more than traditional loans.

"It varies," Seiden said of asset based loan rates. "The healthier the company, the lower the interest rates and costs."

Factors often charge 2 percent a month or an annualized rate of 24 percent, although loans rarely are taken for as long as a year.

In other types of asset-based lending such as asset-based credit lines, lenders rely on the company to pay, while using inventory or receivables as collateral. Rates typically are a little bit above the prime lending rate.

While established firms are turning to factors, new companies are finding that without a credit history or a track record, they may have no choice. "A lot of startup companies can't go to banks," Alibrandi said.

In addition to asset-based loans, firms are finding other types of financing can come in handy during tough times by putting more cash in their pocket up front. Leasing equipment lets firms save money up front compared to outright purchases.

"Credit is so difficult to come by," said Glenn Spiller, president of Syosset-based equipment leasing firm Yooj Solutions. "By leasing you preserve your lines of credit to be used for payroll, growth or expansion or appreciating asset."

Spiller set up a $100,000 lease on imaging software for a radiology group in Westbury. The firm can hold onto money to expand its payroll and pay other expenses.

"Leasing is a wonderful means of growing one's business," Spiller said. "They can write off the monthly payment of the lease."

There also are other ways to get money in a hurry, including borrowing against an insurance policy. But that's a measure that some advisors warn may be short-sighted.

"In an emergency situation, it is available," said Jeffrey Nekrutman, owner of Dynamic Resources, a financial services firm based in Syosset. He said loans taken out against policies can lead to skyrocketing premiums and that failure to pay back loans can jeopardize the entire policy.

"Most permanent policies have loan provisions. But I wouldn't usually recommend it."

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