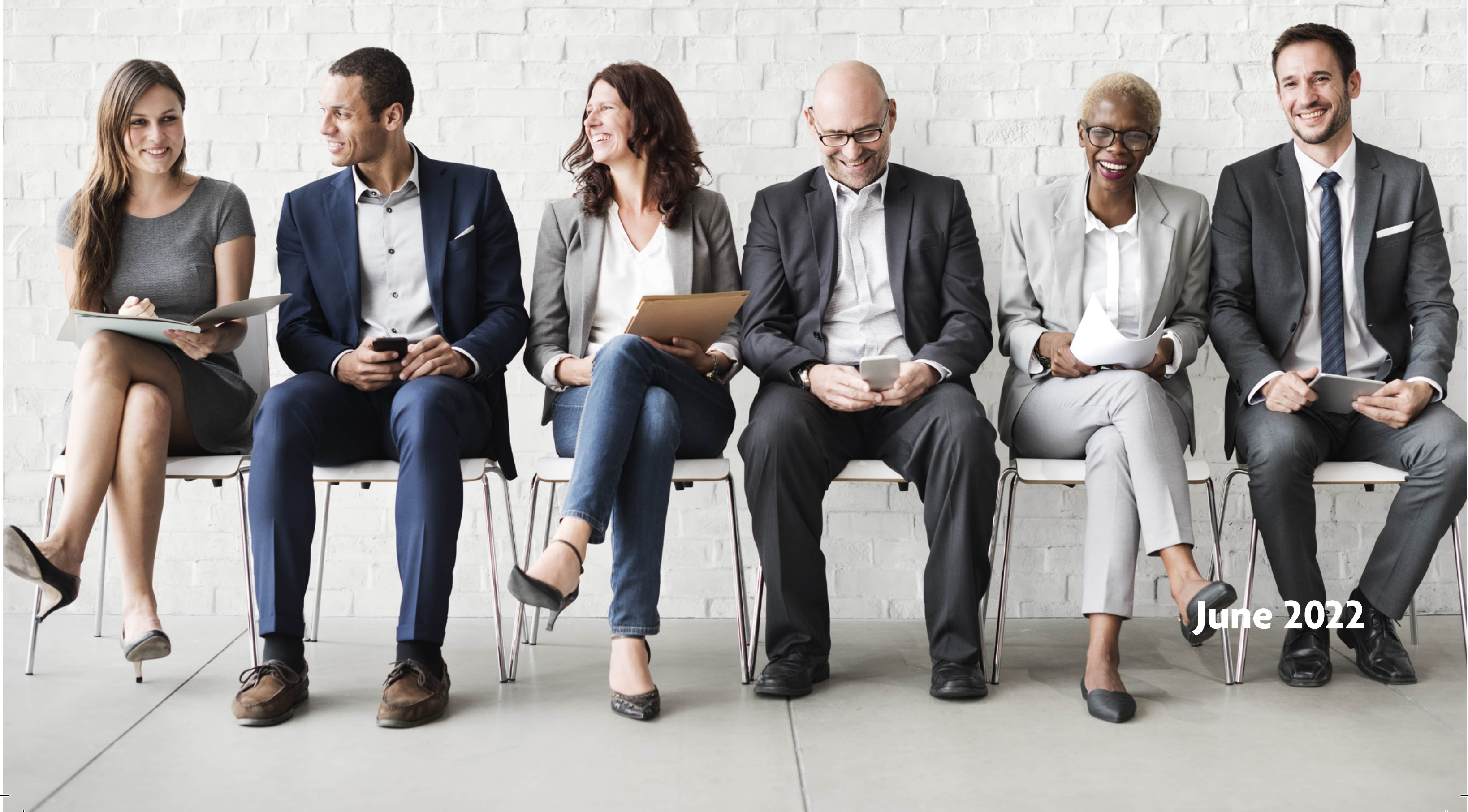
UK FINANCE

GUIDE TO INVOICE FINANCE FOR BUSINESSES AND ADVISORS



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INTRODUCTION

Invoice finance and asset-based lending (IF/ABL) supports UK businesses with £275 billion of sales annually[i]. At any one time, UK Finance's IF/ABL members will be advancing over £18 billion to their client businesses.

Finance has been provided against trade debts since medieval times; the roots of modern 'factoring' are often traced back to the 17th Century textile trade centred around Blackwell Hall in the City of London. But research suggests that the modern products and services that are termed invoice finance and asset-based lending are not always well understood by the people that run businesses and those that advise them.

No type of finance is right for every business. But for many businesses that trade business-to-business on credit terms, invoice finance and asset-based lending can be a sustainable and affordable finance options, unlocking working capital and supporting growth.

This is a brief introduction to the products for business owners and those that advise them. It explains how they work, who provides them, and the standards that they will meet in doing so.

ABOUT INVOICE FINANCE

Invoice finance is the provision of finance to businesses against their accounts receivable or debtor book, represented by their outstanding invoices. Whether your business is currently owed £50,000, £100,000, or £10,000,000 from business customers, invoice finance might be an effective option for your business.

UK businesses often wait an average of 40 – 60 days to be paid, and sometimes longer. Invoice finance provides businesses with the ability to access funds almost immediately after the point of sale, instead of waiting months to be paid.

There are two main types of invoice finance offered in the UK, they are usually referred to as *factoring* and *invoice discounting*. In terms of the principles through which the finance is provided the products are actually very similar. We will cover this and the difference between the two products later.

Around 35,000 businesses currently benefit from invoice finance in the UK and it is an option for the majority of businesses that sell their goods or services to other businesses on credit.

These well-established and flexible forms of finance are a great way of unlocking cash flow for lots of businesses and are used for many reasons, for example:

- For businesses experiencing accelerated growth; the finance unlocked can grow as soon as the business sells more goods or services.
- For a business that is asset-light or has been through a tough time, they provide a great way of accessing finance despite a diminished balance sheet, weakened financial performance or increased liabilities, due to the fact that the main security taken and financed against is the invoices your company raises. Essentially an invoice finance provider will look at the underlying strength of a business, its debtor book and its future prospects, and will not necessarily focus on short-term financials.
- The products are also used by businesses looking to re-structure some or all of their existing borrowings. Depending on the circumstances, invoice finance could provide a way of paying these down whilst also unlocking cashflow.

If you have a solid customer base, you may well find that the levels of finance available could far exceed what you could get through other forms of finance.

Alongside the benefits that the finance itself can bring, invoice finance providers have huge experience and knowledge when it comes to sales ledger management and can offer users of invoice finance great support when it comes to managing cashflow and credit risk.

Invoice finance is quite simple. When a business takes out an invoice finance facility they are able to 'assign' (essentially sell), some or all of the customer invoices that are currently outstanding to the finance provider, and have access to up to 80 or 90 per cent of the value of those invoices virtually immediately. The remaining 20 or 10 per cent of the value of the invoices assigned – less the finance provider's fees - will be made available upon payment of the invoices by the customer of the client business. The customer of a client is often referred to as the 'debtor'.

The invoices raised and assigned generate a 'pot' of available funds. The client is then generally able to draw down the funding it needs within that availability. The availability will track the invoices raised – more invoices will unlock more finance.

More information is available on the UK Finance website at: https://www.ukfinance.org.uk/our-expertise/commercial-finance/invoice-finance-and-asset-based-lending.

About Asset-Based Lending

Often used by businesses with multiple asset types on their balance sheet, including larger businesses, asset-based lending facilities will generally provide finance against the debtor book and supplement it with lending against other specific assets such as stock, plant and machinery, and other types of physical and intangible property (including some types of intellectual property). The debtor book and other assets are used to generate a blended facility limit for the client to draw down from.

Terminology varies but UK Finance would generally distinguish between *asset-based lending* which allows a business to free up working capital from their existing assets and *asset finance* which is used by businesses to acquire assets, usually through hire purchase or leasing arrangements.

Standards in Invoice Finance and Asset-Based Lending

Like many forms of finance that are provided to business clients, as opposed to individual consumers, invoice finance and asset-based lending products and services are not subject to statutory regulation in the UK.

UK Finance represents around 40 invoice finance and asset-based lending providers in the UK. Our members are committed to meeting the highest standards in their dealings with prospects and client businesses. These standards are set out in UK Finance's IF/ABL Standards Framework. This is comprised of three key components:

- **The Code and supporting Guidance** which outlines a number of commitments relating to a set of standards that clients and prospective clients should expect from an IF/ABL provider;

- **An independent Complaints Process** which is available to clients and guarantors. Modelled on Alternative Dispute Resolution services in regulated sector, this is currently independently provided by the Centre for Effective Dispute Resolution; and

- **An independent Professional Standards Council** (PSC) which oversees the Code, Guidance and independent Complaints Process, ensuring that they are up to date and effective. The PSC is also charged with making appropriate recommendations to protect and enhance the reputation of the industry.

If a business chooses to enter a contract with a financier that is not a member of UK Finance, it is important to be aware that the provider will not be bound by these standards, and, in particular, the facility will not be covered by the independent Complaints Process. In the event of a dispute the only right to redress would generally be through a formal legal process.

FREQUENTLY ASKED QUESTIONS

Terminology

A wide variety of different terms are used to describe the products that we describe collectively here as *invoice finance* and *asset-based lending*. *Factoring* is the 'original' and still most widely known term but is often misunderstood, particularly in the UK. It tends to be used to describe the whole industry in other countries, however.

In the UK **invoice finance** is often used to describe both factoring and invoice discounting. Sometimes **asset-based lending** is used but, again, this accurately refers to specific types of facility provided against debts and wider assets (see below). Other terms used - with varying degrees of specificity and, in some cases, accuracy - can include *debt factoring, debtor finance, receivables finance, sales finance* or *supply chain finance*.

Costs of invoice finance and asset-based lending

Used by around 35,000 businesses[ii] in the UK, with over 40 providers supporting over £275bn of invoices, invoice finance and asset-based lending is a very competitive market.

It is worth highlighting that whilst some business owners / managers understand that invoice finance will provide 80 or 90 per cent against the value of their invoice(s), there is also a misapprehension that the remaining 10 or 20 per cent represents the fee charged by the invoice finance provider. This is generally not the case, with the remaining 10 or 20 per cent made available to the client on payment of each invoice.

In most cases, there are two main fees applicable to an invoice finance facility;

- Service Fee - a small percentage of the invoice value charged up front; and

- Discounting Fee - similar to interest and based on how much a business decides to utilise. How much a business utilises of their available funds is usually entirely up to the individual business.

Clearly fees will vary and take into account the risk of non-payment and additional services provided (such as factoring collections). UK Finance members who offer invoice finance are required to ensure that they make prospects and clients aware of all charges applicable, so any business interested in finding out more is encouraged to talk to a variety of providers to find out more.

Sizes and sectors of businesses

IF/ABL providers support businesses of all sizes, from small start-ups to larger corporates. The products are available to businesses in most sectors of the UK economy - any business that trades on credit terms with other businesses is likely to be able to access some type of invoice finance or asset-based lending.

Relationships with customers (debtors)

The majority of invoice finance providers offer both 'confidential' and 'disclosed' facilities. Confidential means that a clients' customers will not be made aware of the finance in the background.

However there is a misconception that the products are *only* for businesses that have challenges and this is certainly not the case. The last two decades have seen an increase in larger and more sophisticated businesses using invoice finance. Annual sales of client businesses supported by Invoice finance in the UK amount to over £275 billion – with the average client generating over £7 million of annual sales. The products are increasingly recognised as mainstream finance options, not just specialist choices.

A specialist invoice finance provider will be able to look beyond the immediate financials to the underlying strength of the business – to its customers and debtor book. This does mean that they will often be able to provide finance in circumstances where other products may not be either possible at all, and to businesses that may be experiencing challenges, but working with a provider that has the expertise in supporting businesses through the good times and the bad is a positive thing.

Speed of funding

Most invoice finance providers have invested in online platforms that enable easy submission of invoices. Funds are often available immediately or within 24 hours of submission of an invoice or invoices.

Invoice finance is highly flexible, and the level of finance available grows in line with the business as well.

Non-payment of an invoice by a customer (debtor).

Research shows that some businesses are concerned about what happens if or when one of their customers does not pay an invoice that has been funded. Regardless of whether an invoice finance facility is in place or not, this can be a difficult time for any business.

In addition to the funding, an invoice finance provider can provide a wealth of knowledge and experience in credit and collections management, which can often help a business in reducing such losses. However if it does happen and the business accessed circa 80% of the value of the unpaid invoice, they will be required to pay the funds back. They would be in no worse position than if they didn't have an invoice finance facility other than having to repay the advance. It is usual that rather than physically having to pay the funds back, any shortfall would be taken by a reduction in future advances, and any short term cashflow issues caused by the loss could be discussed with the finance provider with the aim of minimising disruption.

How complicated are invoice finance and asset-based lending

These facilities do require more active management on the part of a client than simply applying for and drawing down a loan, for instance. But generally speaking they will also be unlocking greater levels of funding. Technology is making the products increasingly light touch – integrating directly with business banking, accounting and invoicing platforms for instance – which in turn is making the products even more cost-effective and accessible.

Single or selective invoice finance

Whilst many providers will provide invoice finance on a 'whole turnover' basis, where the finance provider advances funding against the majority of the debtor book, rather than single invoices by themselves, some providers do offer single or selective invoice finance.

For more information please contact Jennifer Tankard or Alex Waterman at jennifer.tankard@ukfinance.org.uk or alex.waterman@ukfinance.org.uk.

ABOUT UK FINANCE

UK Finance is the collective voice for the banking and finance industry. Representing around 300 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

We work for and on behalf of our members to promote a safe, transparent and innovative banking and finance industry. We offer research, policy expertise, thought leadership and advocacy in support of our work. We provide a single voice for a diverse and competitive industry. Our operational activity enhances members' services in situations where collective industry action adds value.

UK Finance members comprise a diverse range of bank and non-bank providers of finance and other services to business customers. Membership includes the large, specialist, challenger and international banks, as well as non-bank specialist finance providers, including technology-driven providers of financial services. Members provide a wide range of commercial finance products and services from term-lending and overdrafts, to invoice finance and asset-based lending. The list of IF/ABL Members is below.

AIB Commercial Finance Ltd	Lloyds Bank Commercial Finance Ltd
AIB Group (UK) PLC	Metro Bank
Allied Irish Bank	Novuna Business Cash Flow
Aldermore Invoice Finance	Paragon Business Finance PLC
Santander UK Plc	Partnership Invoice Finance
Bank of Ireland UK PLC	Praetura Commercial Finance Limited
Barclays Trade and Working Capital UK & Ireland	Pulse Cashflow Finance Limited
Bibby Financial Services Ltd	Quba Solutions
BNP Paribas Commercial Finance Ltd	RBS Invoice Finance Ltd
Close Brothers	Regency Factors Limited
Cynergy Bank	Secure Trust Bank Commercial Finance
Danske Bank	Shawbrook Bank Limited
eCapital	Skipton Business Finance Ltd
Growth Lending	Sonovate Ltd
Happen Finance Ltd	Team Factors Ltd
HSBC Invoice Finance (UK) Ltd	Time Finance plc
Independent Growth Finance Ltd	Time Invoice Finance Limited
Investec Capital Solutions Limited	Ultimate Finance Group Limited
White Oak	Virgin Money UK Plc
Leumi ABL Ltd	Wells Fargo Capital Finance

Endnotes

i The total turnover of the UK businesses supported by UK Finance's Invoice Finance and Asset-Based Lending (IF/ABL) members was £275,972 million in 2021. This represents around 12.5 per cent of UK GDP.

ii 34,861 UK businesses were supported by UK Finance IF/ABL members as at the end of 2021. Latest data about the IF/ABL sector can be found at https://www.ukfinance.org.uk/data-and-research

DISCLAIMER - *This guide has been prepared solely for the purpose of providing general information relating to invoice finance and asset-based lending (IF/ABL) products. Unless we provide express prior written consent, no part of this guide should be reproduced, distributed or communicated to any third party. For the avoidance of doubt, this guide does not constitute advice (legal, regulatory, financial or other) provided by UK Finance, nor should the reader treat this document as providing anything other than general information. UK Finance (or any of their respective members, officers, employees or agents) shall not have any liability to any person or company arising from or in connection with any use of the guide or any information or views contained therein.*