

THE MONEY GAME

Getting Your Due

Entrepreneurs are trying to take the stigma out of borrowing against receivables

By **SIMONA COVEL**

Data Drive Thru Inc. was on a roll. The Dallas company had received \$1.5 million in start-up money from an angel investor. Its signature product, a tool to transfer data from one computer to another, won an award at a trade show and landed on shelves at big-box stores like Staples.

But the company hit a financial wall in the second half of last year. A second round of angel funding, expected to come in at \$7.5 million, fell through as credit markets froze. The company was too young to have the well-established cash flows needed to get a bank loan, and retail customers were taking longer and longer to pay—as many as 30 extra days in some cases.

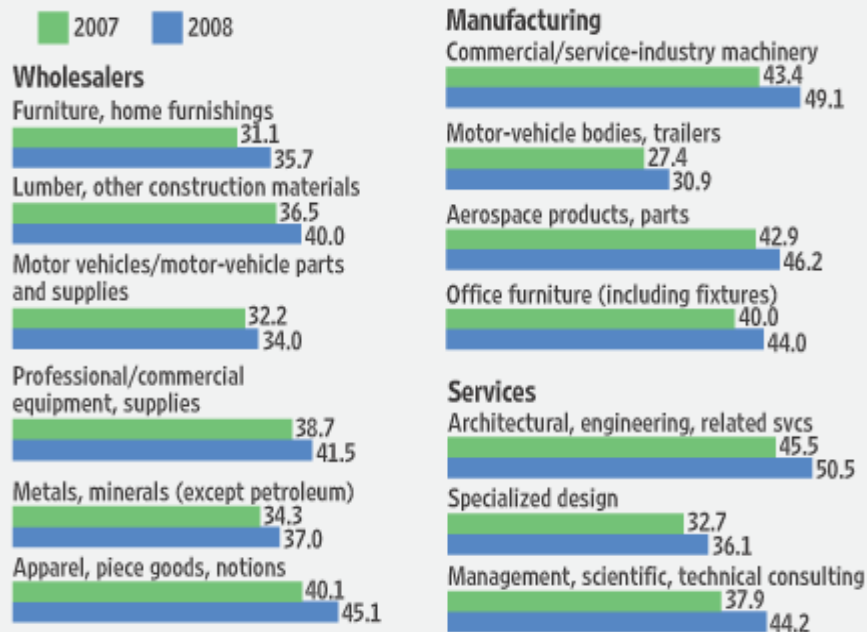
The Journal Report

“Everyone is holding onto cash as much as they can,” Chief Financial Officer Brad Oldham says.

So Mr. Oldham took an unconventional step: He listed the company’s accounts receivable—invoices due to be paid by the big-box stores that buy Data Drive Thru’s products—on a new online auction site called the Receivables Exchange. Anonymous lenders bid on those receivables, agreeing to lend Data Drive Thru money against them and then take a cut when customers pay the bills.

The Check Is in the Mail

Average number of days it takes private companies to collect money owed by customers, by selected industries



Source: Sageworks Inc.

Borrowing against receivables isn’t new. For hundreds of years, cash-strapped people or companies known as factors to advance them funds based on money owed by customers. But with interest rates sometimes exceeding 30% or 40% annually and tales of unsavory business practices, this small corner of finance is considered by many to be a funding source of last resort.

A few companies are trying to change that with products and services designed to make the process of borrowing against customer invoices cheaper and more transparent. These products are gaining ground in the recession as companies—particularly small, untested

ones—find their credit lines cut and other sources of funding gone.

Mr. Oldham had worked with factors before and didn't like the high prices. But he knew Data Drive Thru's receivables were valuable; the company regularly collects hundreds of thousands of dollars from big, well-known office-supply stores. "Retailers may not be real fast paying, but they do pay," he says.

That's the ideal scenario for Receivables Exchange LLC, which launched its first online receivables auction in November. The New Orleans company—executives describe it as eBay for receivables—provides the platform for companies like Data Drive Thru to post their invoices. Lenders then peruse the site, searching for receivables against which they are willing to lend. Lenders bid on those invoices, with the majority electing a fixed buyout price similar to eBay's "buy it now" feature.

The next day, the borrower is wired the money, minus the lender's fee, which might be two, three or four cents on the dollar. Receivables Exchange, which is in the background verifying that the invoices are real, takes a varying percentage commission on each trade.

While the credit crunch has buoyed Receivables Exchange's growth on the borrowing side—the company has 200 customers and says its sweet spot is a firm with \$10 million to \$100 million in revenue—it also has translated into fewer lenders. Exchange co-founder Justin Brownhill says he expected to see 20 times as much demand as supply on the exchange. Instead, with \$7.5 billion in invoices and \$15 billion in available capital, it's about a two-to-one ratio, largely because banks haven't stepped up as much as expected amid their own vast problems...

Getting Big-Company Rates

With buyers anxious to extend payment terms in tough times, some are turning to Atlanta's PrimeRevenue Inc., a supply-chain finance company. PrimeRevenue works with large companies—from car makers to retailers—that want a few extra days to pay their hundreds of small suppliers. Through a network of bank partners, PrimeRevenue will advance the money owed to the small suppliers, at an interest rate that's based on the credit standing of the bigger buyer company—generally a single-digit annual rate, PrimeRevenue says. PrimeRevenue's fee is wrapped into that rate; the rest of it goes to the banks that provide the financing. Suppliers can log into the program, look at their future-dated receivables and either elect to wait for the buyer to pay the bill, or click a button to get an advance.

Small suppliers can't just ask to be in the program, however. The bigger buyer company has to initiate the system and pay a fee to participate. Today, PrimeRevenue services 40 big global companies or units of those companies, up from about 30 early last year.

For small suppliers, the program offers an opportunity to land financing at rates based on the credit quality of their big customers, instead of the higher rates generally offered to smaller companies. When a big industrial customer told executives at metal-stamping company Universal Metal Products about PrimeRevenue, "our initial reaction was skeptical, because whenever you hear of this type of thing you think of some kind of back-room factoring house," says John Rapacki, the Wickliffe, Ohio, company's controller. But the rate was much lower than a factor, and Mr. Rapacki liked the ability to use the system without a fixed commitment. (Universal Metal Products' large customer doesn't want to be named; some participating companies would rather not admit they are extending payment terms.)

The ability to pick and choose when to use the system for financing has proved critical in recent months as rates have marched higher amid uncertainty in capital markets, Mr. Rapacki says. At the beginning of 2008, the interest rate on his receivables was around 3%, and Universal Metal Products would regularly take advances on payment. These days, it is closer to 10%, so the company rarely taps into the financing.

--Ms. Covel is a staff reporter of The Wall Street Journal in Chicago.