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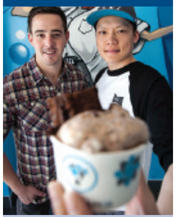
Up Front



These twenty-somethings use liquid nitrogen to make ice cream.
PAGE 3

News & Analysis

By dropping this old packaging, Snak King hopes to get new customers.
PAGE 5

People

How Michael Jones went from AOL to Myspace to the tech incubator Science.
PAGE 13

MAIL TO:

Satellite Provider Circles Content

TV: DirecTV goes 'Rogue' in hope that new drama draws subscribers.

By JONATHAN POLAKOFF *Staff Reporter*

With a cast anchored by film actress **Thandie Newton** and an edgy plot fit for a cable thriller, the producers of TV crime drama "Rogue" feel they have a hit on their hands.

Especially tuned-in to the success of the show is **DirecTV Inc.** of El Segundo, which is co-financing "Rogue" and is part owner of the series. The 10-episode first season will debut exclusively on DirecTV's Audience Network channel early next month.

It's a bold experiment for DirecTV, which backed "Rogue" after looking at data collected about viewing trends in its core 35-54 viewership demographic. It is

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RINGO H.W. CHIU/LABJ

Focused: Chris Long at DirecTV in El Segundo.

RINGO H.W. CHIU/LABJ

Spinoff: Attorney Randy McMurray at the Cochran Law Group's office in Los Angeles.

Making Cases

Ex-partners of Johnnie Cochran spar over name, legacy

By ALFRED LEE *Staff Reporter*

THOSE calling the old phone number for the late Johnnie Cochran's law firm were greeted last week by an attendant saying they had reached the "Cochran Law Group."

But that firm, only months old, is in fact a newly created competitor to the **Cochran Firm** that was founded by the famed civil rights attorney known for his defense of **O.J. Simpson**.

Both practices are run by Cochran's former partners, who have been locked in an ongoing dispute over money and control in the wake of his death in 2005. The dispute worsened last year, and has since spawned two lawsuits, forced the original Cochran Firm's nine-attorney L.A. office into receivership and led one partner to change the locks on the office doors in an attempt to keep his antagonists out.

In December, **Randy McMurray**, the former managing partner of the original Cochran Firm's L.A. office, launched the **Cochran Law Group**

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Oil Companies Don't Dig Tax

ENERGY: Extraction levy may leave California in hole.

By HOWARD FINE *Staff Reporter*

For years, **Hal Washburn**'s oil company drilled exclusively in California. But in recent years, as it's become more expensive to do that here, **BreitBurn Energy Partners LP** of Los Angeles has focused more on Michigan, West Texas and Wyoming.

And if a 9.9 percent oil extraction tax passes the state Legislature, Washburn said that trend will only speed up.

"It would have significant impact on our capital spending plans," said Washburn, BreitBurn's

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Eatery Growth Leads to South

DINING: Cheesecake Factory adds Latin America to menu.

By BETHANY FIRNHABER *Staff Reporter*

Cheesecake Factory Inc. is working to go global, one region at a time.

The restaurant company opened its first international location last fall in the Middle East, and last month announced that it already has decided to expand into Latin America.

The Calabasas company signed a licensing agreement to open at least 12 restaurants in Mexico and Chile in the next eight years, with the potential to open more in Argentina, Brazil, Colombia and Peru.

Please see DINING page 48

SPECIAL REPORT
BANKING & FINANCE QUARTERLY

MATT BEGLEY is among local factors who have long provided short-term, high-cost financing to L.A.'s apparel companies. But increasingly, factors are lending to IT, engineering and even media businesses. Read all about how this specialized lending works and why factors are changing in this special report.

BEGINNING ON PAGE 19

Growth Factors

As banks tightened lines of credit, more companies turned to high-cost, short-term lenders.

BY JAMES RUFUS KOREN *Staff Reporter*

TIMOTHY **Nelligan** was in a jam.

It was about a year ago and his engineering firm, **Katahdin Environmental Corp.**, had been doing well, getting paid by the state and developers to clean up soil and groundwater polluted by old oil tanks.

But those payments were a long time coming and his bank had cut off his line of credit as it tightened lending requirements, leaving Nelligan wondering how he'd make payroll and cover his tax bill.

"I saw disaster," he said. "The ends would not meet. I had the sales but cash flow was a problem."

So Nelligan took out what amounted to a payday loan for his business. **Fast A/R Funding** in Calabasas paid up front for most of the value of Nelligan's accounts receivables, tiding him over until his customers paid.

Fast A/R Funding is a factor, a type of commercial financier that has been little known outside of the apparel world but is now increasingly common in other industries. Factors in Los Angeles say they've seen a big increase in business over the past few years as stricter lending requirements have kept small-business owners such as Nelligan from getting traditional – and cheaper – bank financing.

"In 2008, banks really stopped lending to smaller and even middle-market companies," said **Barry Morganstern**, managing partner of **Tarkus Capital LLC**, a Thousand Oaks firm that advises factors and helps them raise capital. "So companies have turned to factoring for their working capital needs."

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RINGO H.W. CHIU/LABJ

'Several clients sold Mervyn's receivables to Hana. When Mervyn's went bankrupt, we paid full money to our clients. Our lending price is higher, but we provide the credit protection.'

SUNNIE S. KIM, Hana Financial

Continued from page 19

Downtown L.A.'s **Hana Financial Inc.**, for instance, did nearly $2 billion in factoring deals last year, about 30 percent more than in 2010. And executives at the L.A. office of **Rosenthal & Rosenthal Inc.**, a New York factor, say they've doubled their business here over the past three years.

The past several years have been boom times for factors and other nonbank commercial finance companies. Between 2007 and 2011, factors and nonbank financiers saw business grow 47 percent nationwide, according to **Sageworks Inc.**, a financial analysis firm in Raleigh, N.C.

"Factoring has emerged as a viable financing option in recent years, particularly for rapidly growing companies," said Sageworks analyst Tim McPeak.

How it works

Factors buy a company's receivables – bills owed by other businesses – or lend money and hold receivables as collateral, letting businesses get cash today for payments they are to get in the future. They also provide credit protection and other services. Factoring deals vary in form and cost, but generally work like this:

A clothing manufacturer sells $1,000 worth of shirts to a retailer, who agrees to pay for the goods in 30 days. The manufacturer sells that invoice to a factor for less than face value. A typical discount might be 2 percent, but they vary widely, from a quarter percent to 6 percent or more.

The factor, like the retailer, has 30 days to pay.

But because it now owns the invoice, the factor is responsible for collecting payment from the retailer. After 30 days, the factor owes the manufacturer the agreed-upon amount. With a 2 percent discount, that's $980.

If the retailer goes bankrupt or otherwise doesn't pay, the factor – not the manufacturer – takes the loss. Factors take that risk because, before buying an invoice, they check the credit of the business that will be paying the bill. Large factors might have credit files on 100,000 or more businesses, from big retailers to mom-and-pop storefronts.

In some cases, a factor only performs credit checks on the retailers that buy the goods, collects payments and take a percentage in return – a kind of outsourced credit and billing department. Using those services saves clients money by eliminating the need for some back-office staff and by keeping bad debt off their books.

When factors provide financing, it's a bit more complicated. Typically, a factor can immediately pay the manufacturer up to 80 percent of the value of an invoice. Once the retailer has paid, the factor gives the client the rest of the money – minus interest.

Upon giving an advance, factors usually charge fees or interest that can range from 1 percent to 5 percent per month. Annualized, that's between 12 percent and 60 percent.

"It's not a cheap form of money," said Katahdin's Nelligan, who pays about 2 percent a month on advances. "But I exhausted my options and this is what I ended up executing."

Largely because of those high fees, the factoring industry has a reputation for exploiting desperate business owners.

In one of the industry's more salacious incidents, Los Angeles Police Department detectives in the mid-1990s linked an Orange County factor to the murders of several clients or former clients.

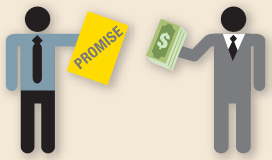
One victim, the owner of a recording studio, owed more than $1 million and was allegedly forced to take out a $2.5 million life insurance policy – payable to factor Coleman

A Factor in the Local Economy

An example of how factoring works.

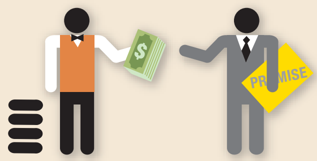
DAY ONE

1. An apparel company sells $1,000 worth of T-shirts to a retailer.
2. The retailer promises to pay the $1,000 within 30 days.

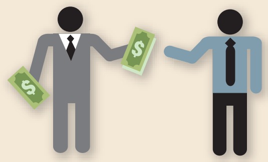


3. The apparel company sells that promise (an invoice) to the factor.
4. The factor advances the apparel company $800.

WITHIN 30 DAYS



5. The retailer pays the factor the full $1,000 from the promise.



6. The factor pays the apparel company the remainder of the original $1,000, minus the factor's fees. In this example the apparel company receives $180.

> **‘It’s not a cheap form of money. But I exhausted my options and this is what I ended up executing.’**
>
> TIMOTHY NELLIGAN, Katahdin Environmental Corp.

Allen. He was later shot to death, police believe, by a hit man Allen hired. At the time, LAPD detectives likened factoring to a legal form of loan-sharking. (Allen died soon thereafter of natural causes; no charges were ever filed against him.)

Edward Von Leffern, a management lecturer at Cal Poly Pomona and an adviser at the **California Small Business Development Center** in Long Beach, said he cautions businesses about using factoring.

“If one of my clients is offered factoring, I want to read the contract as there are many hidden items that are unacceptable,” Von Leffern said.

Michael Baum, an attorney with **Resch Polster & Berger LLP** in Hollywood who has represented factoring clients, said there are plenty of ways for factors to squeeze extra money out of a deal.

For instance, Baum said some deals allow a factor to continue charging a client interest even after their receivables have been paid. Instead of paying interest for 30 days, the client might pay 32 or 35 days.

“Often, clients don’t understand what their true cost is,” he said. “The first time I ever read a factoring contract, the thing might as well have been written in Chinese.”

But Baum and Von Leffern also said that if other kinds of financing aren’t available and a fair deal can be worked out, factoring can be a useful tool.

“Often it comes down to how well a small business can negotiate pricing and terms,” Von Leffern said.

A few banks including Wells Fargo and Carson’s **Merchants Bank of California** offer factoring, but generally factors serve clients that banks can’t – smaller businesses with fewer assets to borrow against.

“Not everyone can qualify for a bank loan,” said **Wade Francis**, president of bank consulting firm **Unicon Financial Services Inc.** in Long Beach. “They don’t qualify for unsecured lending and they don’t qualify for a mortgage on their building because most businesses are renting. Bottom line a lot of businesses could disappear pretty quick.”

Self defense

Blaine Waugh, national sales manager for Redondo Beach factor **Riviera Finance LLC**, said he frequently confronts the notion that factoring is somehow unsavory.

“People will say, ‘Factoring is so expensive. I can’t believe businesses use you guys. It’s usury,’” he said. “All they see is the annualized cost. It’s frustrating.”

But he and other factors defend their rates, saying their fees cover the cost of checking customers’ credit, collecting and processing payments, and compensating them for taking on the risk that a customer won’t pay.

“Is it expensive? Damn right,” Waugh said. “We take a lot of risk.”

Sunnie S. Kim, chief executive of Hana Financial, said many of her clients sold clothes to department store Mervyn’s, which filed for liquidation in 2008. Without Hana or another factor, those clients would have either lost money or had to try to collect from Mervyn’s in bankruptcy court, which factors do in their stead.

“Several clients sold Mervyn’s receivables to Hana,” Kim said. “When Mervyn’s went bankrupt, we paid full money to our clients. Our lending price is higher, but we provide the credit protection.”

She and other factors also note that, unlike banks, which can raise capital for loans by accepting low- or no-interest deposits, factors typically have to pay for their money, either from private investors or in the form of bank loans. That means they have to charge higher rates if they want to have a margin for themselves.

Despite the cost, there’s plenty of demand. Factors Chain International, a factoring network in Amsterdam, the Netherlands, reports that about $105 billion in factoring deals were done in 2011, above the previous peak of $100 billion in 2008.

New business

As major retailers struggle, factors that work in the apparel and manufacturing industries say they’ve seen more businesses interested in the credit protection they provide. Fashion firms want to make sure that if **Sears Holding Corp.**, **J.C. Penney Co.** or smaller retailers go under, they don’t lose money or end up as creditors in a bankruptcy case.

“A couple of major retailers have begun to post challenging results,” said **Kevin Sullivan**, western regional manager for Wells Fargo Capital Finance, a unit of San Francisco’s **Wells Fargo & Co.** that offers factoring. “As that’s happened, we’ve seen companies gravitate toward that credit protection offering.”

He said Wells Fargo’s factoring volume has grown by about 50 percent nationwide over the past five years and should hit about $30 billion this year.

Still other factors have grown by reaching into new industries. A decade ago, nearly 90 percent of Hana’s business was in the apparel

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SPECIAL REPORT BANKING & FINANCE QUARTERLY

> 'With the economy we're coming through, show me a company that hasn't had a loss in the last three years. ... Two or three years of losses don't scare us.'
>
> SYDNEE BREUER, Rosenthal & Rosenthal

Continued from page 21

industry, but now it's less than 70 percent, despite big growth for Hana. Kim said she now works with clients who make toys, electronics and auto parts, as well as temp agencies and other staffing businesses.

"The apparel and textile business is saturated already, but there are many businesses in need of credit protection on their receivables," she said. "We have clients providing nurses to hospitals, clients who do cleaning for big hotels. Any business that has receivables can be a prospect."

Fast Pay Partners LLC, a Beverly Hills factor founded in 2009, works exclusively in the digital media industry, providing funding to clients paid by corporate advertisers such as Atlanta's **Coca-Cola Co.** and Cincinnati's **Procter & Gamble Co.**

Riviera Finance has long provided factoring to trucking companies – another industry where factoring is common – but now does about half of its business with companies providing catering, private security and other services.

Waugh, Riviera's national sales manager, said one of Riviera's fastest growing markets is oil and gas. It's an industry where factoring makes sense: Lots of small businesses, from water haulers to drillers to staffing agencies, get paid millions of dollars by giant oil companies that take a month a more to send checks.

"Most of the money comes from 10 or 15 giant players, and most pay in 60 days," he said. "They're not a problem in terms of credit, it's just a matter of when they pay."

Market shakeup

Hana and other larger factors have also grown as they've taken customers away from New York's **CIT Group Inc.** Once the nation's largest factor, CIT has continued to lose billions in factoring business since its 2009 bankruptcy reorganization. The company got in trouble when it started diversifying from factoring and got into subprime mortgages.

The company's factoring volume – the dollar value of its deals – fell from $45 billion in 2007 to $25 billion in 2012, a 44 percent drop.

"When they had problems, a lot of clients said, 'We can't rely on CIT,' so they started going to places like Rosenthal and Hana," said **Anthony Callobre**, a partner in the banking and finance practice of downtown L.A. law firm **Buchalter Nemer**. "A lot of growth has been at the expense of CIT."

Hana's Kim said she has picked up former CIT clients over the past few years, as did Sullivan at Wells Fargo.

Though their factoring volume has continued to drop, CIT executives say they have started to bring former customers back to the fold.

"The restructuring is three years behind us. From my perspective, it's a rear-view mirror," said **Jon Lucas**, president of CIT's trade finance division. "We've been successful in bringing a lot of our business back."

But even smaller factors, ones that don't compete with CIT, have picked up business as the market for their services has expanded. Across the board, factors say they've been helped by the tighter bank-lending requirements that have made it more difficult for small businesses to get loans.

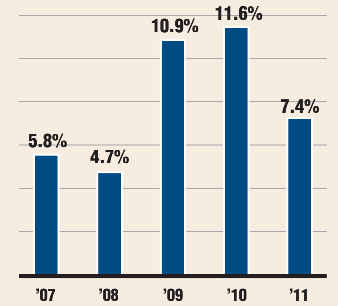
In June, banks headquartered in Los Angeles County had $1.16 billion in commercial and industrial loans of $250,000 or less on their books, according to the Federal Deposit Insurance Corp. That's an improvement over the previous two years, but still down 29 percent from June 2007, when those loans topped $1.62 billion.

Sydnee Breuer, a senior vice president in the Woodland Hills office of Rosenthal & Rosenthal, said factors can work with businesses that banks shy away from.

"Banks want two to three years of profitability," she said. "With the economy we're coming through, show me a company that hasn't had a loss in the last three years. In and of itself, two or three years of losses don't scare us."

Factoring Growth

Percentage sales growth for factors and similar commercial finance companies.



Source: Sageworks

All that opportunity is driving more companies into the factoring business. There are few regulations or barriers to entering the industry, and it might take as little as $1 million in capital from friends and family to start up a small factoring shop, said Tarkus' Morganstern.

Morganstern was co-founder of the International Factoring Association, a Pismo Beach trade group. The association has grown its membership by between 5 percent and 10 percent annually in each of the past few years, said **Bert Goldberg**, the group's executive director.

"There are a lot more people getting into factoring than there are leaving," he said.

Factors and other commercial finance companies saw their profit margins grow from just over 9 percent in 2009 to more than 13 percent in 2011, according to Sageworks, but those numbers are likely on the way down as factors say they are charging lower rates and fees amid increased competition.

Factors that just a few years ago could charge annualized rates of 20 percent or 30 percent might be willing to settle for 14 percent today, said **Bob Zadek**, an attorney in the San Francisco office of Buchalter Nemer who specializes in factoring. That means it might be tougher for new factors to make a go of it.

"There are a gajillion lenders," he said. "I help a factoring company get started every month. I start by trying to talk them out of it."

SPECIAL REPORT BANKING & FINANCE QUARTERLY

Seeking Clients Who've Never Heard of Factoring

By JAMES RUFUS KOREN *Staff Reporter*

SEARCH for "factoring" on Google and you won't find much about **CIT Group Inc.** or **Wells Fargo Capital Finance**, two of the country's biggest factoring firms. But you will find an ad from tiny **Fast A/R Funding**.

Unlike other factoring companies, which get much of their business through sales calls or referrals, Fast A/R is looking for business through online advertising. It's a move that speaks to the kind of businesses Fast A/R wants to help finance: ones that haven't worked with a factor before and might have no idea what factoring is. They might not even know the word.

RINGO H.W. CHIU/LABJ

> 'They'll find us if they search for "factoring." But they might also be searching for "How to make payroll" or "How to get cash for my business."'
>
> MATT BEGLEY, Fast A/R Funding

"They'll find us if they search for 'factoring,' " said **Matt Begley**, chief executive of Fast A/R's since its founding two years ago. "But they might also be searching for 'How to make payroll' or 'How to get cash for my business.'"

Begley's company is one of a new breed that's helping push factoring, a financial tool used largely by apparel companies and other makers of consumer goods, into other industries, accounting for some of factoring's recent growth.

Most of Fast A/R's clients are service providers, such as IT consulting firms, social media developers and commercial cleaning companies. Beverly Hills factor **Fast Pay Partners LLC** is more narrowly focused, working with businesses exclusively in the digital media industry. Both companies use a type of factoring different from the so-called nonrecourse factoring that's common in the apparel trade.

In nonrecourse factoring, a factor purchases a client's accounts receivable at a discount and then collects the receivables. Because the factor, not their client, owns the receivables, the factor does not have recourse to seek payment from the client if a bill isn't paid. That protects the client against bad debt.

But Fast Pay and Fast A/R don't offer such credit protection. They're both recourse factors, meaning they can collect from their clients if their customers don't pay. Though such deals are often structured as the purchase of accounts receivable, they're more easily understood as short-term loans, with accounts receivable held as collateral.

"We're simply a very specialized form of collateralized lending," said **Jed Simon**, chief executive of Fast Pay. "We're not offering credit protection. Our clients are certain they're going to get paid. Their customers are large advertisers employing big ad agencies. The challenge isn't credit risk; it's accelerating the payment."

Cash up front

Fast Pay and Fast A/R are both trying to fill gaps in the commercial finance market, looking for specific types of clients that usually can't get bank lending but that might not see factoring as an obvious choice.

For Fast A/R, that includes small-business owners who aren't familiar with factoring and in years past might have financed operations by taking equity out of their homes.

Aiming to make the process simple, Fast A/R developed its own software to put the factoring process online, from the application to submitting invoices. Fast A/R's system also integrates with QuickBooks, an accounting software program commonly used by small businesses.

Simon

Fast Pay, meanwhile, targets digital media companies in need of advance payment. Unlike most small businesses, those companies might have the option to raise money from venture capitalists or other investors. But **Jed Simon**, Fast Pay's chief executive, said his company allows digital media companies to grow without additional investor money.

"Once your product is built and your technology is there, you shouldn't have to raise equity to manage the working capital shortfall," Simon said. "That's a problem you should use debt to solve."

Jen Sargent, chief executive of Santa Monica's **HitFix Inc.**, said that's why her company has been working with Fast Pay for about a year.

HitFix produces videos and news reports about the entertainment industry for its website and distribution on Hulu and YouTube. TV networks and movie studios buy ads, but they often take three or four months to pay. HitFix could run out of cash while waiting.

"We can have half a million or more tied up in receivables, which is a lot of cash for a business our size," Sargent said. "But it would be a shame to raise funding and give away ownership for a receivables issue."

Fast Pay will pay HitFix up front for up to 80 percent of the value of its receivables. Once its advertisers pay, HitFix gets the rest of the money, minus Fast Pay's fee. Usually that's between 1 percent and 2 percent, depending on the value of the deal and other variables.

Unlike many businesses that use factoring, HitFix also had the option to get a traditional loan, with offers from two different banks that would have charged lower interest rates.

But Fast Pay was ultimately cheaper. At any given time, HitFix is waiting for between $500,000 and $1 million in receivables to be paid. For that amount, it didn't make sense to go with a bank loan, which Sargent said would have come with about $30,000 in legal fees, annual audits and other added expenses.

"If we got to a point where we were financing millions of dollars a month, the math on the bank loans probably look better," she said. "But in the in-between phase, Fast Pay was a much more palatable option."

SPECIAL REPORT BANKING & FINANCE QUARTERLY

Factoring Spreads From Its Traditional Industries

By BETHANY FIRNHABER *Staff Reporter*

FACTORING is a well-worn form of financing in the apparel manufacturing world and most companies accept the high charges as a basic cost of doing business.

Jon Levine, a 25-year veteran in the apparel industry and principal of L.A. consulting firm **Apparel Advisors**, said every fashion company he has ever advised has used a factor. Most distress calls he gets are from struggling apparel companies that don't yet use a factor.

"People call me when they're having problems, and it's usually because they don't have a factor in place and they're trying to collect on their own receivables," he said. "It can be a mess."

Apparel companies have long used factors for two main reasons: to borrow money against invoices they need cash to fill, and to guarantee and collect payment for shipped goods.

Downtown L.A. apparel company **Evy of California Inc.**, which designs and imports kids' clothing and sells it to mass-market retailers such as **Macy's Inc.**, **Target Corp.** and **Wal-Mart Stores Inc.**, uses New York factor **Rosenthal & Rosenthal Inc.**

Evy Chief Executive **Kurt Krieser** said his company uses a factor primarily to help pay for orders that could run into millions of dollars in advance of receiving payment from big customers.

"The majority of our customers are mass retailers, so, generally speaking, although our payment terms are 60 days, by the time they process everything it can be longer than that," he said. "We could have a line of credit with a bank, but that would require either substantial equity or substantial collateral, and we'd just rather collateralize our borrowing with our receivables."

But hiring a factor is more expensive than other forms of financing, particularly for businesses that manufacture products for small retailers. That's because factors are more concerned with the creditworthiness of the retailers they will ultimately solicit payment from than with that of the borrower.

In the apparel industry, Levine said finance terms in factoring agreements vary depending on the size and dependability of end retailers, but that factors generally allow companies to borrow against up to 80 percent of invoice totals and charge between 1 percent and 3 percent to run credit checks and guarantee payment.

RINGO H.W. CHIU/LABJ

'Competitive Edge': Bill McConnell at Compass Transportation in Wilmington.

Faster payment

He said the benefits of using a factor outweigh the cost. A factor guarantees payment, which is important in the event a retailer goes bankrupt. In that case, manufacturers who don't use a factor would have to fight for payment or lose the money. There are also other benefits.

"It's somewhat advantageous to use a factor because stores tend to pay factors before companies that don't use factors," he said.

Those benefits are part of the reason why a growing number of businesses in other industries, such as temp agencies and trucking companies, also look to factoring.

Wilmington trucking company **Compass Transportation** began working with **Orange Commercial Credit**, a factor out of Olympia, Wash., about 10 years ago.

Bill McConnell, president of Compass, said factoring gives his company a competitive edge.

"This is a cash-flow business. If a customer approaches me and asks if I can handle an extra $20,000 in work a week, a lot of companies my size would say they can't," he said. "The only restriction I have to growing is: Can I get the equipment? Not: Can I fund the receivables?"

Calabasas factor **Fast A/R Funding**, which tends to factor for small to midsize service providers rather than manufacturers, recently began working with San Diego health care technology consulting firm **Ideal Health IT**.

John Brimble, president and chief executive of four-year-old Ideal Health, said factoring has been integral to his young company's early success.

"Our business is in a fast-growth sector and factoring is definitely something that helps us facilitate that," he said. "Larger, more established companies may be able to use some other financing options, like lines of credit, but that's not generally the case with smaller, newer, fast-growing firms like us."

Some companies that use factoring while they're small might decide once they've grown much bigger to manage cash flow with a line of credit from a bank and handle customer credit checks in-house. But Apparel Advisors' Levine said he thinks setting up that kind of operation is more effort than it's worth.

"It's a business decision a company has to make," he said. "But honestly, I think that if factoring is working, you just negotiate the fees."

That's why Evy's Krieser said he'll continue to use a factor.

"I find factoring, for us, to be very cost-effective," he said. "It makes my business easier to run and I can spend more time focusing on what my business is rather than on the financing of the business."

Staff reporter James Rufus Koren contributed to this article.

Ancient Practice Found Fertile Ground in L.A.

By HOWARD FINE *Staff Reporter*

FACTORING is one of the oldest forms of finance. The ancient Babylonians and Romans used factors. The word "factor" means "he who gets things done" in Latin.

The use of factoring spread in England during Elizabethan times. Factors in Europe helped finance the fledgling Massachusetts Bay Colony established by the Pilgrims in 1620.

"The history of factoring is the history of commercial finance in America," said **David Tatge**, an attorney at the Washington law firm **Epstein Becker & Green PC**, author of 2010 book "American Factoring Law."

> **'(By 1900), the factor ... emerged as a commercial financier and purchaser of its client's receivables, while also making loans against the security of client-owned inventory.'**
>
> DAVID TATGE, in his book 'American Factoring Law.'

Through the 18th and 19th centuries, factors acted as sales agents for manufacturers, receiving goods on consignment mostly from European textile companies and selling them here. They paid the manufacturers most of the sale price up front, then paid the rest – minus their own fee – when the buyer paid.

After the Civil War, as large apparel and textile companies took shape in America, factoring companies started focusing domestically. That intensified in the 1890s as steep tariffs were enacted on a wide swath of European goods.

By 1900, American apparel and textile companies were mass marketing their products nationwide, finding their own customers in the process. That turned factors more into financiers.

"The American factor no longer acted as a commissioned sales agent," Tatge says in his book. "Instead, the factor now emerged as a commercial financier and purchaser of its client's receivables, while also making loans against the security of client-owned inventory."

Factors also assumed the credit risk if the end customers did not pay or were late in paying, defined as "nonrecourse" in financial terms. In addition, they performed the bookkeeping and collection work on behalf of the manufacturer.

The first half of the 1900s saw the establishment of several prominent factoring companies that still exist, including **CIT Group Inc.** (founded in 1908), **Heller Financial** (1935) and **Rosenthal & Rosenthal Inc.** (1938).

The industry exploded in the 1930s, with the dollar volume of goods factored topping $1.1 billion by the start of World War II, according to figures that Tatge cites.

Shady image

By the 1950s, factoring companies branched out into new industries, including cosmetics, chemicals, glass, electrical appliances and furniture. Other types of receivables lenders also had come along: asset-based lenders that don't assume title to those receivables as factors do, and recourse factors, who differ from traditional factors because they leave greater risk with the manufacturer.

The total volume of factored goods reached $3.5 billion by 1955.

From the 1960s through the 1980s, waves of consolidation swept through the factoring industry, resulting in a number of the largest factors being controlled by major banks.

But the entry of the new players, especially some of the recourse factors, eventually led to the spread of the perception of factoring as an industry with shady elements. Some of the smaller, less-established recourse factors had limited access to financing themselves and charged their clients higher fees, sometimes more than 50 percent on an annualized basis. That led to the perception of factoring as a financing tool of last resort only for the most desperate of companies.

Tatge's book refers to 1987 articles in the Wall Street Journal and Fortune magazine that express the perception:

"Historically, the factoring business has a smell about it, usually because firms that sell off receivables have tended to be strapped for cash. To get quick money, they sell their accounts receivable to last-resort lenders, typically at steep discounts from face value."

Tatge rebuts this perception, noting that the American factoring sector since then has expanded into a huge industry, reaching $135 billion in volume of factored goods in 2007, according to a survey from the **International Factoring Association** in Pismo Beach. He told the Business Journal that recourse factors now account for about 25 percent of that volume; the other 75 percent are nonrecourse factors that take the hit themselves if end customers don't pay or pay late.

L.A. market

The L.A. area, with its high concentration of apparel and furniture manufacturers, has long been fertile ground for factors. Tatge said established companies such as James Talcott, CIT and Walter Heller set up shop here in the 1950s and 1960s. Several smaller factoring companies also opened in the area, including **Milberg Factors** and **Capital Business Credit**.

Local banks, such as Security Pacific Bank and Crocker National Bank then entered the market through acquisitions. More recently, in 1999, **Wells Fargo Bank** also entered through acquisitions.

"The Southern California market, with its apparel concentration, has long been very competitive for factors," said **Robert Zadek**, of counsel to the San Francisco office of L.A. law firm **Buchalter Nemer**.