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Accounts receivable financing enhances cash accumulation

What if you could use other people's money to unlock your dormant assets, placing it on the compound growth curve and paying only simple interest – and at the same time protect your business from creditors and lawsuits?

Why wouldn't you use it?

Every day, businesses across the country generate accounts receivable balances by selling goods and services to their customers.

The seemingly immeasurable value of accounts receivable is consistently generated and replenished on the business' balance sheets.

The challenge the business faces is that these balances normally do not appreciate and sometimes take a long time to collect. An innovative financial strategy may be available to use this ubiquitous business asset to produce significant opportunities for business owners.

This concept uses other people's money without interrupting the flow of accounts receivable. While this was originally designed to work with physicians who typically carry large medical receivables, it has now evolved to work with most business owners.

The strategy is called accounts receivable financing. Banks or other lending sources may loan the business money based on its annual average accounts receivable balance. This is not to be confused with factoring or selling your accounts receivable balances, which can result in losing control or a reduced value of the receivables.

With accounts receivable financing, normally a simple interest payment is made on this loan. The business owner can use this money as a bonus for himself or to other key employees and purchase a financial product that will grow on the compound growth curve.

A misunderstanding people have is thinking the

Guest Column



Alan Lockhart

simple interest loan rates may exceed the return crediting rate which could eliminate the value of this program.

The reality is that due to the effects of compounding, the program can still produce significant positive cash accumulation over time, even in an inverted interest rate environment.

If you compare past history, when loan interest rates climb, normally the crediting rates of a well-positioned asset will increase proportionally. This increases the value of compounding interest. The longer this interest rate arbitrage is in place, the greater the growth in the spread.

A few examples of businesses that have benefited from accounts receivable financing include accounting

firms, chiropractors, consulting firms, law firms, dentists, engineering firms, funeral homes (pre-need), auto dealerships, manufacturers and physicians.

Not all companies will benefit or qualify for this program, so it's important to work with a CPA and financial adviser. The ideal candidates are businesses who have strong cash flow and have a need to fund their retirement or want to offer executive benefits to key employees.

Other strategies are business buy/sell agreements and business succession planning.

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Simple vs. Compound Leveraged Investment Comparison

This illustration assumes a loan amount of \$500,000, an interest-only loan rate of 8.5 percent, an investment yield of 8 percent, and a tax rate of 30 percent.

Year of Participation	Without Tax Deduction		
	Simple Interest	Compounded Investment Value	Net Gain from Compounding
1	\$42,500	\$540,000	(\$2,500)
5	\$212,500	\$734,664	\$22,164
10	\$425,000	\$1,079,462	\$154,462
15	\$637,500	\$1,586,084	\$448,584
20	\$850,000	\$2,330,478	\$980,478
25	\$1,062,500	\$3,424,237	\$1,861,737
30	\$1,275,000	\$5,031,328	\$3,256,328

Year of Participation	With Tax Deduction		
	Simple Interest	Compounded Investment Value	Net Gain from Compounding
1	\$29,750	\$540,000	\$10,250
5	\$148,750	\$734,664	\$85,914
10	\$297,500	\$1,079,462	\$281,962
15	\$446,250	\$1,586,084	\$636,834
20	\$595,000	\$2,330,478	\$1,235,478
25	\$743,750	\$3,424,237	\$2,180,487
30	\$892,500	\$5,031,328	\$3,638,828