

Why Haven't I Heard of Factoring Before?

You have, but it's not typically referred to as factoring. Accepting credit cards as a method of payment in retail transactions is a form of factoring.

Let's say you use your credit card to buy a pair of sunglasses from Mr. J's Sporting Goods. When your credit card is swiped, Mr. J receives a deposit into his bank account, but the amount he receives is not the total amount of the sale. A fee of 2% to 5% is deducted by the credit card company for advancing Mr. J the cash against your promise to pay your credit card bill.

The credit card company is the factor in this scenario, but the big difference is that they charge a fee to the merchant as well as the customer. Unlike Visa® or MasterCard®, invoice factoring companies do not charge your customers interest.

Factoring has been in practice for centuries. Traders had to fund their trips to distant lands in order to bring back goods that were in high demand, such as spices or silk. Wealthy patrons would advance traders the money they needed to make the round trip, knowing that when they returned, the goods would sell quickly and the trader would repay the advance.