THE FULL SPECTRUM

A Publication of SPECTRUM Commercial Services

COLLATERAL LIQUIDATIONS:
The First in a Three Part Series Focusing on Liquidations of Accounts Receivable, Inventory & Equipment

Liquidating Accounts Receivable—Some General Guidelines

A/R is Strong Collateral - Asset-Based lenders generally find that a company's accounts receivable are typically the quickest and, generally, most reliable source of repayment of a working capital loan. However, in a serious default scenario resulting in an imminent liquidation, there are certain steps that the lender should take to ensure the collectibility of the A/R. Most important is the need to stay alert, recognize and document loan defaults and don't delay in taking specific collection actions in those cases where your trust in the borrower has been violated.

Be Proactive – Get Info. From Your Borrower - The key is to be proactive. You will need to know each of your borrower's customers (called "*account debtors*" in the Uniform Commercial Code). Obtain the latest *detailed* accounts receivable aging along with the most recent customer contact list containing mailing addresses, phone numbers and contact names. If possible, obtain copies of all outstanding invoices owed by your borrower's customers and all pertinent back up information (purchase orders and shipping evidence) and begin concentrating on each account. If that is too difficult, at least obtain the largest invoices as they often represents a significant portion of outstanding accounts Going forward, if the company will remain operating for some period of time, insist on copies of all future invoices and the appropriate backup.

Notify the Customers of Your Loan - Under the UCC, once an account debtor receives written notification that your bank has a collateral interest in the accounts receivable, the customer is *obligated* to send payments directly to your bank, in your bank's name. If they nonetheless send payments to the borrower, the payment is not effective to satisfy the obligation. Under the law, they could be forced to pay those invoices a second time to you.

Within 24-hours of a default, the lender (and not the borrower) should send out a notification letter to all of the borrower's current (and any future) customers directing them to send all payments to the lender. Although the notice must include the bank's signature, we've found it helpful to include the signature of the borrower as well, if available, to provide customers assurance that the payment instructions are endorsed by their vendor-your borrower. The letter should include a detailed list of the amounts owed by the customer but nonetheless instruct that ALL payments be sent directly to the bank.

You should use certified mail, return receipt requested, and/or FedEx or other reliable overnight delivery service for larger account debtors to prove receipt. For example: those accounts with balances greater than $25,000 use FedEx, balances of $5,000-$25,000 use certified mail and for those under $5,000 use regular mail. Remember your loan is collateralized by these receivables and therefore you need to give these notices priority. A delay in the notification process will potentially have a negative impact on your ability to effectively collect out on the receivables in question if payments are received by the borrower and never reach you.

Resolve Customer Disputes and Make Collection Calls - Once notices are sent, you can expect some phone calls from customers with questions or payment disputes. Verify with your borrower any discrepancies their customers bring to your attention. Even in liquidation, your borrower is still your best first resource to clarify any discrepancies encountered. A day or two after the notices are sent, make collection calls to verify receipt of the notices by the customers, to verify the amounts owing, and to confirm that the customer understands that payments are to be directed to your attention.

Prioritize your efforts by concentrating on the higher dollar receivables with your initial collection efforts. At all times be aware of and document any outstanding credits or potential off-sets that may be or are claimed by a customer. Then have your client help you understand these items. When necessary, send out stronger collection letters to those hard to collect customers. Lastly, remember to maintain detailed notes on each customer as to who you spoke with, what was discussed and when the discussion occurred. SPECTRUM typically utilizes a spreadsheet by customer/debtor to memorialize these conversations and collection efforts.

Act Quickly and Decisively - The key in collecting on A/R is to act quickly and with urgency. Receivables make strong supporting collateral for a loan because they turn quickly. However, this same quick turning nature of A/R can mean there will be nothing left to collect if you don't act with diligence and urgency in a liquidation scenario.

SPECTRUM – Your Bridge For Those Hard to Finance Credits

SPECTRUM continues to assist banks by financing existing credits that have suffered a setback, credits in transition and new potential credits that are currently outside the bank's parameters. SPECTRUM can provide the financing bridge for these struggling credits until they return to stable and profitable operations.

SPECTRUM Programs:
As the source for working capital for non-bankable credits, SPECTRUM's product lines remain a strong fit to address the many issues encountered with struggling credits.

- For those smaller and/or severely financially stressed companies, an **Accounts Receivable Financing** accommodation may be the best fit.
- For the larger non-bankable credits with relatively stronger performance, better internal controls and more experienced management, our **Asset-Based Lines of Credit** product may be better suited. Within this program we focus on financing receivables, inventory, equipment and R.E.
- SPECTRUM also offers a unique product called our **Structured Asset-Based Line of Credit** for those credits needing to leverage various collateral classes but who lack the required financial performance and internal controls necessary to qualify for our typical Asset-Based Line of Credit. This program is basically a hybrid program combining an **Accounts Receivable Financing** accommodation for the A/R with an **Asset-Based Line** on inventory, equipment and/or real estate.

Participation Opportunities:
SPECTRUM continues to offer participation programs that not only benefit the client but the bank as well.

- The bank can choose our **Pro-Rata Participation Plan** whereby the credit will benefit from a blended Bank/SPECTRUM interest rate.
- Under SPECTRUM's **Guaranteed Participation Plan**, the participant bank enjoys SPECTRUM's unlimited corporate guarantee in addition to a first collateral position on all of the borrower's assets. With these strong credit enhancements, the bank makes a solid loan while also acquiring the operating accounts and enjoying the ability to cross sell other bank products. Ultimately, the bank can maintain a relationship or acquire a new one rather than pushing away a potential customer. Further, under this very popular program the participating bank *can ask to be paid out of its participation at any time for any reason, no questions asked.*

Given the variety of SPECTRUM financing programs, we would like to encourage you to give us a call the next time you encounter a **Hard to Finance Credit** and let SPECTRUM put a finance package together that will best suit your client.

<u>Thank You!</u>

Our business comes from your referrals. All of us at SPECTRUM would like to thank you for the referrals you send us.

Give us a call and allow SPECTRUM to be a part of your portfolio solution!