

Achieving Bank Readiness for **Asset Based Lending**



A Comprehensive Checklist for ABL Clients by TAB Bank

Asset-based lending offers businesses a valuable way to unlock capital by leveraging existing assets, such as accounts receivable, inventory, or equipment. However, before entering underwriting, companies should aim to be “bank ready” to meet the standards established by TAB.

While many businesses may already know the process, it can be challenging to understand what is needed when starting the journey to be approved for an ABL. This document outlines the key financial processes, controls, and systems necessary to prepare your business for an ABL loan with TAB Bank.



1. Understanding the ABL Framework

Unlike traditional loans that focus primarily on credit history, ABL is secured by tangible assets. TAB’s underwriting team evaluates:

- **Eligible Collateral:** The quality and age of accounts receivable, the valuation of inventory, and the marketability of equipment can qualify these assets as collateral.
- **Borrowing Base Calculation:** TAB will review how much you can borrow based on the eligible collateral (e.g., eligible invoices multiplied by an advance rate).
- **Risk Factors:** Customer concentration risks and the aging of invoices is a primary concern for TAB’s team. The bank will analyze the age of your invoices, focusing on those that are less than 90 days old, as well as the total number of customers the business serves.



2. Critical Financial Record-Keeping Processes

A recurring challenge among prospective ABL clients is the absence of financial record-keeping. To be bank-ready, your financial processes should include:

a. Detailed Accounts Receivable (A/R) Management

- **Eligibility Calculations:** Our clients need to be able to determine which invoices qualify based on set criteria (e.g., age and customer reliability).
- **Customer Concentration Analysis:** Our clients need to be able to understand what percentage of their total A/R are concentrated with a few customers. A concentration exceeding 25% warrants closer examination to better understand the impact on the business.
- **Timely Updates:** Our clients can implement processes and systems to ensure that receivables, payables, and accounting entries are made on time.

b. Payment Application and Matching

- **Payment Allocation:** Have a documented process for how incoming payments are applied to outstanding invoices.
- **Invoice Matching:** Ensure that payments are matched correctly to invoices to maintain accurate A/R balances, which is critical for calculating your borrowing base.

c. Calculation of Key Metrics

- **Borrowing Rate and Advanced Rate:** Understand and be able to calculate the formulas that determine your borrowing base (e.g., the subtotal of eligible assets multiplied by the advanced rate).
- **Financial Ratios:** Maintain a standardized template for key financial ratios that lenders review during underwriting.



3. Business Financial Reporting Systems

TAB Bank's confidence in your business is directly tied to the sophistication of your financial reporting:

a. Production of Financial Statements

- **In-House Capability:** Ideally, your business should be able to produce monthly financial statements. This shows consistency and internal financial control.
- **Outsourcing Options:** If internal capabilities are lacking, consider outsourcing this function. However, the frequency must remain monthly to meet TAB Bank's expectations. Fractional CFOs are a good option for smaller companies that might not be able to justify the expense of a full-time CFO.

b. Audited Financials and Field Exams

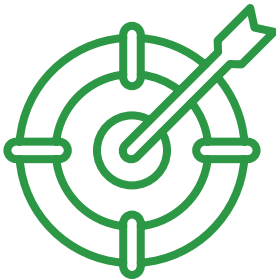
- **Audited Reports:** TAB will require reviewed financial statements for most ABL credit facilities. Audited statements are usually required for loans greater than \$8 million.
- **Field Exams:** Be prepared for lender field exams that assess your internal controls and financial procedures. Make sure your controls and procedures are documented.



4. Internal Financial Controls and Accounting Expertise

While many clients have a small finance and accounting team, TAB Bank does expect a level of financial sophistication and internal control. To help you know if your business is ready for an ABL, review the following:

- **Accounting Team:** Does your business have a dedicated accounting team or professional who manages your financial records? Smaller companies may only need basic accounting, while companies seeking a loan over \$5M should have a CFO.
- **Accounting Controls:** Does your team currently implement and document accounting controls to ensure accuracy and reliability in your financial reporting?
- **Regular Reviews:** Is your team willing to have annual reviews and, when applicable, third-party audits to help demonstrate that the business's financial practices are sound?



5. Meeting Covenants and Strategic Planning

TAB Bank and similar lenders set specific covenants that your business must understand and adhere to. Key considerations include:

- **Covenant Adherence:** Document your processes for monitoring and create a spreadsheet to monitor all loan covenants.
- **Cash Flow Projections:** Demonstrate that you have sufficient cash flow to cover expenses. If current cash flow is lacking, provide a realistic, data-driven plan showing how cash flow will improve in the short term.
- **Business Strategy:** TAB looks for a "real story" behind the numbers. A well-articulated business strategy, particularly when dealing with inventory, equipment, or invoice financing, can make a significant difference.



6. Considering Factoring as an Alternative

For companies that lack the internal systems or sophistication required for traditional ABL:

- **Factoring or A/R Financing:** This can be a viable alternative, especially for businesses with limited back-office capabilities. Factoring involves selling your A/R to a third party in exchange for immediate cash, often without the stringent covenant requirements.
- **Simplified Paperwork:** If your systems are not developed enough to support ABL underwriting, submitting basic paperwork and a schedule of A/R for factoring may be a more appropriate solution.



7. The Bank-Ready Checklist

To summarize, here is a concise checklist that any business should review before applying for an asset-based loan:

Monthly Financial Statements: Ensure you can produce up-to-date financial statements, whether internally or via an outsourced provider.

- **Audited Financials (if applicable):** Have third-party audits in place for companies at higher revenue levels.
- **Accounts Receivable (A/R) Calculations:** Maintain detailed records showing which invoices are eligible (preferably under 90 days) and understand the borrowing base calculation.
- **Customer Concentration Analysis:** Monitor and document the risk associated with high customer concentration.
- **Payment Matching Processes:** Have systems in place to match payments to invoices accurately.
- **Standardized Financial Ratios:** Utilize template formulas for key financial ratios to facilitate reviews.
- **Dedicated Accounting Team:** Ensure an accounting function is in place, scaled appropriately to your company's size.
- **Internal Controls and Covenant Understanding:** Demonstrate strong internal controls and a clear understanding of any loan covenants.
- **Clear Business Strategy and Cash Flow Projections:** Present a solid plan for addressing any cash flow issues and articulate your overall business strategy.
- **Consideration of Factoring Alternatives:** If internal systems are lacking, explore factoring as a potential alternative.

We Believe In You and Your Business

While the above information is helpful to understand if your business is “bank ready,” it can not be overstated how much TAB values clients who are willing to make a plan and work as a team with our ABL experts.

While bigger, more traditional banks may have tighter credit boxes and stricter covenants, here at TAB Bank we value a financial team's ability to plan and improve cash flow. The purpose of Asset-Based Loans is to provide businesses with the needed capital to maintain operations and grow.

Ensuring your business is “bank ready” and that you have a financial plan in place will help your business get needed funding more quickly. Whether you are producing your financial statements or opting for a factoring solution due to limited internal capabilities, being prepared is key to unlocking the capital you need.



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