

The History of Factoring (thousands of years, in 35 slides!)

**International Factoring Association
Annual Meeting, April, 2012
© 2012, David B. Tatge and
Jeremy B. Tatge**

This presentation has been provided for informational purposes only and is not intended and should not be construed to constitute legal advice. Please consult your attorneys in connection with any fact-specific situation under federal law and the applicable state or local laws that may impose additional obligations on you and your company. Attorney Advertising

EPSTEINBECKERGREEN

The Historic Roots of Factoring

- Factoring Began:
 - A. Around the birth of Christ
 - B. When Bert Goldberg was born
 - C. With the Mesopotamians, about 2,000 B.C.
 - D. In the Roman Empire
 - E. During the Holy Roman Empire, in the Middle Ages

Mesopotamia

- Was a trading society:
 - A. In Egypt
 - B. In Israel
 - C. Found where the Tigris and Euphrates rivers flow, i.e., modern day Iraq, together with parts of Syria and Turkey
 - D. In India
 - E. Found in Bob Zadek's imagination

Early Mesopotamian Commerce:

- The roots of factoring, at least in the sense of merchants who purchased trade receivables, at a discount, start here
- Local merchants hired commission agents to travel to far away cities, to buy goods, and bring them back, for resale by the merchant
- Merchants made cash advances to the agent, who gave the merchant a negotiable promissory note. The note might be payable to the individual merchant, or to a “tamkarum,” a guild of merchant-bankers who specialized in trade
- The merchant could borrow against the agent’s note from the tamkarum, or sell it to the tamkarum. If the note was sold, always at a discount, the right to the ordered goods passed with it, to the tamkarum

Other Early Financiers

- Middlemen in ancient Babylonia, who leased land from the owner(s), and extended trade credit to tenant farmers. These middlemen also supplied seeds, plows and tools, and bought the crops, once grown
- Written tablets of the period, around 500 B.C., show that receivables from these activities could be assigned
- The Sophist Protogoras, in Greece, chosen in 444 B.C. to write laws for the people of Athens. Among these laws was the approval of credit
- Roman factors – Claudius, for example, raised money from Roman factors to finance a winter harbor, in Ostia

Medieval England

- Factoring, as we know it today, was clearly established in medieval England.
- The center of this activity was:
 - A. Guild Hall
 - B. The Inns of Court
 - C. Blackwell Hall
 - D. Customhouse Wharf
 - E. Frederick House (Alan's ancestral home)

Blackwell Hall

- Blackwell Hall was the center of the English cloth trade
- The early English cloth industry was founded by Flemish immigrants, from Yorkshire and other Northern counties, who settled there under the protection of a decree of King Edward III of May 1, 1326. The same decree held that only royalty, nobles, and prosperous merchants could wear colored clothes.

Blackwell Hall, cont'd

- Blackwell Hall, built in 1297, was licensed by King Richard II to several local mercers, in 1397.
- A mercer was:
 - A. A dealer in expensive fabrics
 - B. A cloth maker
 - C. A merchant
 - D. A lender

Blackwell Hall cont'd

True or False?

- Members of the Cloth guild who operated in Blackwell Hall pitched (displayed) their wares:
 - A. Under Placards
 - B. At Stands
 - C. At Rests
 - D. By placing merchandise on rugs

Blackwell Hall cont'd

Factors who worked at Blackwell Hall –

- A. Had an exclusive monopoly
- B. Sold to Drapers and other local merchants
- C. Sold to foreign factors
- D. Extended credit to clothiers (cloth makers)
- E. Traded in wool themselves
- F. Some of the above
- G. All of the above

Blackwell Hall cont'd

Factors at the Hall were regulated, in 1623, by:

- A. The London City Council
- B. The Privy Council
- C. Parliament
- D. John Beckstead
- E. None of the above

Blackwell Hall cont'd

After 1677, factors at Blackwell Hall were regulated by:

- A. Mike Ullman
- B. The King
- C. The governors of Christ's Hospital
- D. The Archbishop of Canterbury
- E. None of the above

Blackwell Hall cont'd

- Over time, the factors began to serve as middlemen, displacing the clothiers, on the one hand, and the merchants and drapers, on the other, so that they no longer communicated directly with one another.
- The growing economic clout of the factors at Blackwell Hall created resentment
- The factors traded in wool, finished cloth, and extended credit to strapped merchants
- Around 1720, they also began to assume credit risk

Blackwell Hall cont'd

- One disgruntled clothier, in 1739, called Blackwell Hall Factors:
 - A. Useless drones in the human hive
 - B. Thieves and knaves
 - C. Scum of the earth
 - D. Men of sound commercial mind
 - E. #####!

Blackwell Hall Factors

- Were widely known. Everyone of the period knew who a Blackwell Hall Factor was, and what such a person did
- Compare today. What friend (or relation) of yours can tell you what a factor does?
- Blackwell Hall Factors trained young American factors, sent from the Colonies
- Had other roles; for example, commissioners in bankruptcy, akin to a bankruptcy trustee today
- Bought, sold and leased land

English Factors Worked On The Continent, Early On

- For example, Claes-Olof Livijn's "Studies in Financial History" refers to a factoring transaction in 1441, between an English merchant and his factor, sent to Brittany "William Warwyke of Salisbury, Merchant...sende into Bretayn [in Brittany] Wauter Trenchevyle, his Servant, Factour and Attorney, to Merchandise ther with wollen Cloth".

Factor's Assumption of Credit Risk

- A factor's fee, at common law, for assuming credit risk on client accounts, was called:
 - A "risk commission"
 - A "guarantee commission"
 - A "del credere commission"
 - "A gold commission"
 - Something else

Del Credere Commissions

- Apparently, arose about 1720, on the Continent.
- Came from the Italian factoring practices, of Lombardian bankers; means guarantee, or warranty (of the solvency, of the client's account debtor)
- Ray Westerfield's book, *Middlemen in English Business Particularly between 1660 and 1760* (Yale Univ. Press, 1915), quotes a 1721 letter, written in Dublin, which said there were a great number of London merchants "who were solely maintained by Foreigners in Holland, France and other nations by Factorage at 2 ½%"
- Del credere commissions ranged from ½ to 5%, with 2.5% being common. Therefore, one can assume that del credere commissions may have existed in 1721
- Without question, del credere commissions were common in commercial trade, and are referenced in English case law, by the 1780s
- These commission came to NYC, around 1814, after foreign manufacturers tired of taking large losses on export sales to America.

Factoring in England Extended Beyond Textiles

- In Britain, Corn factors and Hop factors also plied their trade, for example
- In terms of insured capital, in England, in 1770, Blackwell Hall factors were first, Corn factors second, and Hop factors third.
- By 1820, the situation was reversed, with Corn factors being first, Hop factors second, and Blackwell Hall factors, third

Factors Outside of England

Factors were found in all the major trading nations:

- Holland, Portugal, France, Spain, Germany, Russia, etc
- The Dutch were described by Voltaire as the “factors of the world”
- And, they were found in all of the Colonies of the major powers: Goa, in India (Portugal), Jamaica, Antigua, etc. (Britain), Timor and New Amsterdam /New York (Dutch), Peru (Spain), the Hanseatic League (Germany).

Summarizing, Factors, At English Common Law, and Elsewhere:

- (1) Were commissioned sales agents
- (2) who held and advanced against consigned inventory, generally, at 50-70%, often for a principal merchant located overseas;
- (3) accepted credit risk, by guarantee of the collection of local sales made by the merchant principal, and
- (4) performed other functions, such as ledgering debt and collecting from the account debtors.

Factors flourished anywhere that trade over long distances created delays and risks

American Factoring

Factoring came to America:

- A. During the Civil War
- B. With the Pilgrims, in the 1620s
- C. Shortly after the Revolution
- D. About 1700
- E. None of the above

American Factoring

The first factors physically based in America were located in:

- A. Boston
- B. Baltimore
- C. New York
- D. Savannah
- E. Philadelphia

American Factoring cont'd

Early American Factors in NY City did NOT include:

- A. Herman LeRoy
- B. David Jencks
- C. Isaac Iselin
- D. Thomas Achelis
- E. Frederick Vietor
- F. Casimir de Rham
- G. Gilbert & John Aspinwall
- H. The Brown Brothers
- I. Charles Graebe
- J. Louis F. Dommerich

One Modern American Factoring Company Traces Its Founding to:

- A. 1808
- B. 1812
- C. 1827
- D. 1835
- E. None of the above

The Roots of America's Largest Commercial Factor Today (CIT)

1790: *LeRoy, Bayard & McEvers*

Herman LeRoy was the Dutch General Counsel in New York and the founder of the firm LeRoy, Bayard & McEvers. His daughter married Daniel Webster. His partner, William Bayard, was a close friend of Alexander Hamilton.

1808 *deRham, Iselin & Moore* (later, A. Iselin & Co. and William Iselin & Co.)

Isaac Iselin was a Swiss immigrant, in 1801. Hired 1805 by LeRoy, Bayard & McEvers at age 18 to work as their supercargo (agent) on the ship Maryland (outbound from NY); later a partner in the firm, from 1808-1815. Isaac married a French-Swiss wife, Aimee Jeanne Susanne Emilie Roulet in 1810. He represented the silk and glove industries of Lyon, France. He was subsequently a partner of *DeRham, Iselin & Moore* from 1815 – 1835. Isaac returned to Basel, Switzerland in 1835, but came back to New York after the Great Fire of 1837, to restore the firm. He returned to Basel in 1839 and died there. His son was Adrian Georg Iselin, founder of A. Iselin & Co. Isaac's grandson was Adrian Iselin, Jr., a director of The Guaranty Trust from 1892-1910. Adrian's son, William, founded *William Iselin & Co*, acquired by *CIT* in 1931.

Other Early Factors of New York:

1825 Charles Graebe arrives from Germany, later partners with Frederick Vietor, who immigrated about 1828, and Thomas Achelis, his cousin. They form *Frederick, Vietor & Achelis* in 1843, with offices in NY, Bremen, Chemnitz, Lyon and Paris

1827 *Rusch & Co.* (Swiss & German mills)

1833 *Brown Brothers* (Liverpool, Baltimore, NY); later, Alex Brown & Sons, Baltimore, and Brown Brothers Harriman & Co., Boston. US Sup. Ct. case, 1840

1839 *Auffmordt & Co., Inc.*

The First American Born Factor

Started business in 1854. He was:

- A. Henry Ittleson
- B. Mitchell Rogers
- C. Walter Heller
- D. James Talcott
- E. John P. McGuire

Modern Factoring in America Arose

- A. From 1890 - 1905
- B. From 1854 – 1865, under Talcott's tutelage
- C. In 1904, in St. Louis
- D. None of the above

The Modern American Factor

Arose from 1890 – 1905.

- The McKinley Tariff of 1890, on European imports, was 49.5%
- American factors stopped acting as sales agents for European manufacturers, i.e., selling from consigned inventory on site
- American mills started to have their own sales forces
- American factors began to serve diversified industries, beyond textiles (toys, shoes, furniture, etc.)
- American factors became commercial financiers, of client accounts receivable, purchasing the accounts (in old-line factoring), or lending against them. No longer simply financing consigned inventory in the factor's possession

1910 - 1944

- Rise of the asset-based lenders, starting when CIT was founded in 1908. Other early ABL's: Mercantile Credit Co. of Chicago, later, Continental Credit Trust (1908), Commercial Credit Co. (1920, Baltimore) and Walter Heller & Co. (1920, Chicago)
- CIT goes public, 1924; James Talcott & Co. does so, 1935-1936
- First wave of consolidation, and “national” factors, as the asset-based lenders all moved to acquire factoring companies, from 1928 – 1935
- Advent of factoring lien laws (1911 – 1950)
- Benjamin Milberg starts Milberg Factors (1936)
- The biggest commercial finance companies who own factors in 1936 are CIT and Commercial Credit; the two biggest independents are L.F. Dommerich & Co. and James Talcott, Inc. CIT's factoring volume is \$245 MILLION
- Rosenthal & Rosenthal is founded by Imrie Rosenthal(1938)
- The Assignment of Claims Act of 1940 helps fund World War II
- James Talcott, Inc. is still primarily an “old line” factoring company, in 1944. It begins lending in the early 1940s, but in a very small way

1945 - 1960

- Banks enter factoring around 1945 (First National Bank of Boston, Trust Co. of Georgia)
- US factoring volume, 1948, is \$2.5 BILLION. Compare 1936, when CIT's volume was \$245 million, and total volume was probably \$500 million or so
- 1954 – The UCC is drafted. Adopted in almost all States by the mid1960s
- 1955 – Volume of Asset Based Lending (\$4.9 Billion) exceeds factoring volume (\$3.7 Billion) for the first time

1961-1990

- U.S. style factoring is re-exported to England (1960)
- 1965-1970. Banks enter factoring in a big way. Also, Walter E. Heller & Co. and First National Bank of Boston move into international factoring
- 1969 – Standard Factors Co. buys Sterling National Bank (which factors today via Sterling Factors)
- Factors push into new industries, sometimes, with horrible results
- “Maturity factoring”, where the factor’s clients are at the wholesale stage of the business cycle, i.e., the client’s account debtors are manufacturers or distributors, and the factor pays on the average due date (maturity) of accounts purchased during the month, becomes less common. Account debtors of factoring clients become, principally, retailers, and the factoring is either on a straight “collection factoring” basis, without advances, or on a collection basis coupled with factor advances to the client on the date of purchase (“advance factoring”)
- A second wave of banks entering factoring, 1980-1985
- American factoring volume falls to less than half of world volume. Between 1985 and 1990, domestic factoring volume rises 8.4%, while international volume rises by 22%

1990 to Date

- Entry into factoring of some industrial giants (GE Capital, General Motors)
- Inception of niche factors (for example, Health Capital Investors, Inc., formed 1994, which factors healthcare receivables)
- Banks continue to acquire factors (for example, BB&T buys Phillips Factors in 1997; Wells Fargo buys Century Business Credit, in 1999, Capital Factors, owned by Capital Bank of Miami, is sold to Union Planters in 2004)
- An explosion of smaller factoring companies, who purchase accounts principally on a full recourse basis
- Continued development of the international market
- A major rise in technology (factoring via cloud based platforms, client access to factor's server via the world-wide web, web-based marketing, etc.)

Conclusion

As this brief overview shows, factoring is, in a broad sense, The History of Commercial Finance in America (or, at least, a very large part of it)