GE Capital
Commercial Finance

Guide to Asset Based Lending

Prepared by GE Capital Commercial Finance, Inc.

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Introduction

Welcome to the Guide to Asset Based Lending. GE Capital—the world's largest asset based finance company—has prepared this guide to help you better understand asset based lending and the many ways businesses can benefit from this type of financing.

The guide explains asset based lending through a series of questions and answers. The first section lists all of the questions in order—basic issues are covered first, and more technical issues later. Scan the list to find questions that address issues of interest to you, then go to the Questions & Answers section for the corresponding answer.

A Glossary section defines terms you may encounter in the guide and in the asset based lending industry. For those interested in learning more about GE Capital, a section called GE Capital Resources includes brief descriptions of our many services.

While you use this guide as a key source into the world of asset based lending, we also welcome your feedback. If you have questions or ideas for enhancing the guide, please send us an e-mail through our website at http://www.gecommercialfinance.com.

Asset Based Lending

List of Frequently Asked Questions

Asset Based Lending

Questions and Answers

1. What is a revolving credit facility ("revolver") and how does it work?

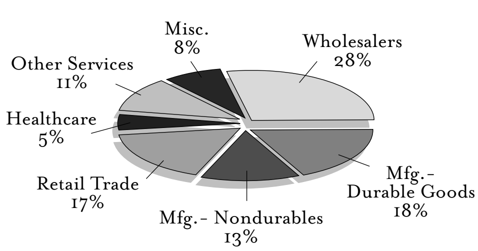
A revolver is a loan which can be drawn down and repaid. In a business context, a revolver frequently is secured by the borrower's receivables and/or inventory. This kind of asset based loan is designed to optimize the availability of working capital from the borrower's current asset base.

Here's how it works. The borrower grants a security interest in its receivables and/or inventory to the lender as collateral to secure the loan. This grant of security interest creates the borrowing base for the loan. As receivables are paid, the cash is turned over to the lender to pay down the loan balance. When the borrower needs additional working capital, the borrower requests another advance.

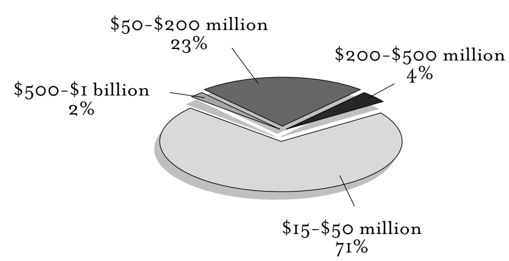
The lender manages a revolving credit facility and the related collateral in order to offer the borrower the largest possible loan amount at any given time. Because the borrower's customers are generally *not* notified of the assignment of the accounts to the lender, the borrower continues to service its receivables. The borrowing arrangement is usually transparent to the borrower's customers.

2. Is asset based lending such as a revolver a common type of financing?

Absolutely. According to the Commercial Finance Association, asset based lending is over a $200 billion market. The users of asset based lending span a broad range of industries, with manufacturers representing approximately 31% of the total marketplace, followed by wholesalers (28%), and retailers (17%). By revenues, the large majority of these borrowers (71%) are under $50 million in size. (See charts for additional details.)



Asset Based Borrowers
by Industry



Asset Based Borrowers
by Revenue Size

3. What is the principal advantage of using a revolver secured by receivables and/or inventory?

The principal advantage is the acceleration of cash flow to the borrower to support its working capital needs. By using its current assets as collateral, a company is able to generate cash sooner than if it had to wait for inventory to be sold to become accounts receivable and accounts receivable to be paid in cash. Cash is available as needed, and any cash not needed on a daily basis is used to pay down the loan balance and minimize interest expense. A revolving credit facility is actually a very cost-efficient alternative for a business that needs to liquify its working capital without having to slow growth or add to its equity capital.

4. Why do companies use revolving credit facilities?

Companies generally take the secured revolver alternative when they cannot obtain an unsecured bank loan which, when added to their normal cash flow, would satisfy their working capital needs. In these circumstances, a secured revolver may provide adequate incremental cash acceleration to fund ongoing business operations.

5. What kinds of companies use revolvers?

Many different kinds of companies use revolvers. They are particularly popular among retailers, wholesalers, distributors, and manufacturers because these types of companies (a) can benefit from a cost-effective source of working capital, and (b) have specific types of current assets that can easily be pledged as security.

6. Do publicly traded companies use revolving credit facilities?

Absolutely. Publicly held companies use revolvers for the same reasons any company uses them—to accelerate cash flow. As the capital markets continue to grow and the IPO market continues to operate efficiently, increasing numbers of smaller companies gain access to the public equity markets. Even newly public companies use revolving credit facilities to optimize the use of existing assets to provide working capital. A revolving credit facility often provides a much lower cost source of working capital than raising additional equity.

7. How does a revolving credit facility differ from a term credit facility?

The outstanding loan amount with a revolver secured by receivables may fluctuate on a daily basis. With a term loan, the outstanding amount is fixed for a period of time, such as a month or a year. A term loan generally provides for an agreed upon payment schedule, and amounts paid on a term loan generally cannot be reborrowed. In contrast, a revolver allows the borrower to borrow, repay, and reborrow as needed over the life of the loan facility.

There are advantages to both revolvers and term loans depending on the borrower's needs. The structure of revolvers provides a great deal of flexibility for borrowing and repayment. Most companies secure a revolver with current assets, such as receivables and inventory, and use the borrowed funds to finance working capital needs. In contrast, companies tend to secure term loans with fixed assets, such as property and equipment, and use the borrowed funds to finance longer term needs and additional capital equipment.

8. What is a borrowing base?

A borrowing base is comprised of the assets, generally inventory and/or accounts receivable, which are available to use as collateral to secure a revolver. The size of the borrowing base varies with changes in amounts of the borrower's current assets. For example, as the borrower builds or acquires new inventory, or as it generates fresh receivables from new sales, these assets are covered by the security interest and generally would be eligible for inclusion in the borrowing base.

9. Why does the lender monitor collateral in a revolving credit facility?

Ongoing monitoring of the collateral helps to maintain a business relationship on a basis that benefits both borrower and lender. By keeping track of the type and quality of collateral in the borrowing base, a lender can make available to the borrower the largest possible loan which can be supported by the collateral.

10. What is the cash collection cycle and how does it work?

The cash collection cycle is simply a way of segregating collections as accounts are received. As receivables are paid, the cash collected is used to pay down the outstanding loan balance. This creates a win-win situation: the lender minimizes the outstanding loan risk, and the borrower minimizes idle cash and interest expense while creating renewed borrowing availability. When the borrower requires additional cash for working capital, the lender advances funds based on the updated borrowing base. This cycle can be done as frequently as daily if needed.

11. What receivables are eligible as security for a revolving credit facility?

Most receivables from completed transactions are eligible. Some receivables which fall into specific categories, however, are not. Typical examples of ineligible receivables would include receivables 90 or more days past due and any intra-company receivables. Some lenders also have the capability to lend against certain government receivables and foreign source receivables.

12. What inventory is eligible as security for a revolving credit facility?

Treatment of inventory varies from company to company and from industry to industry. It would not be unusual for eligible inventory to include all finished goods and marketable raw materials. It would be much less common to include work in process, damaged goods, slow moving inventory, or certain specialized products that can only be sold to a limited number of purchasers.

13. What is dilution?

Because of factors such as warranty returns, bad debt write-offs, and incorrect invoices, not all invoices generated are ultimately collected. Dilution is the difference between the invoices generated and the cash actually collected, expressed as a percentage of the total. For example:

A company has $1,000,000 in invoices.
$950,000 is collected ($25,000 is returned goods and $25,000 is subtracted for prompt payment discounts).
The difference is $1,000,000-$950,000 = $50,000.
The rate of dilution is $50,000/$1,000,000 = 5%.

14. What is the advance rate?

The advance rate is the maximum percentage of the current borrowing base that the lender can make available to the borrower as a loan. Consider an example using inventory. If a given inventory consists of 25% raw material, 10% work in process, and 65% finished goods, then up to 90% the gross inventory (everything except work in process) would be considered eligible. Assuming a 50% advance rate on eligible inventory, loan availability would amount to 45% of gross inventory (50% of 90% = 45%). Actual figures will vary by company and industry, and will depend upon the individual facts and circumstances.

15. How does a lender determine the appropriate advance rate on eligible receivables?

A common rule of thumb in the finance industry for determining the advance rate on receivables is 1 minus 2 times the rate of dilution, plus 5%:

Advance Rate = 1-[(2D) + .05], where D is dilution

If dilution is 5%, the advance rate is 85%:

Advance Rate = 1-[(2 x .05) + .05] = 85%

In determining the advance rate, a lender may also look at factors including receivables turnover and the borrower's overall receivables management.

16. How does a lender determine the appropriate advance rate on eligible inventory?

An advance on eligible inventory may be affected by its type (raw materials, work in process, finished goods), its age, how quickly it turns, and how effectively the company tracks and controls it. Many lenders seek advice regarding the appropriate advance rate from outside appraisal firms that specialize in assessing the collateral value of inventory goods. The borrower may work with the appraisal firms and the lender to help them better understand the market for the collateral inventory, helping to maximize the collateral value and, therefore, the size of the loan.

17. Can I have a revolving credit facility if I don't have receivables?

Yes. It is possible to have a revolving credit facility secured solely by inventory, although advance rates are generally not as high as for facilities secured by receivables. Inventory-only facilities are commonly used in the retail industry, where most cash sales are generated from inventory.

18. Can I have a revolving credit facility secured by inventory in different countries?

It may be possible to use the inventory as collateral to support a U.S.-based revolving credit facility, depending on which country the assets are located in, and provided the assets are owned by a U.S. parent company or a company domiciled in the U.S. In an increasingly global marketplace, a growing number of businesses cross borders to service customers or source inventory. Not all revolving credit lenders can offer cross-border facilities and few can offer a borrower a foreign revolving credit facility. If your needs involve cross-border facilities, ask about a lender's cross-border capabilities before accepting any proposal.

19. Do all industries use asset based lending secured by receivables or inventory?

No. Some businesses may not have the accounts receivable or a tangible inventory traditionally associated with asset based lending. For example, a hotel may have receivables from its clientele but most asset based lenders would not consider these receivables as eligible collateral. A company in the heavy construction business may be entitled to receive progress payments as a project is built, but these progress payments are not receivables in the pure sense; should the project not be completed or the work stopped, the lender might not be able to collect the accounts. Different industries have different kinds of collateral depending on the business they are in, and in each case the collateral must be evaluated on its own merits.

20. Does asset based borrowing add new cash to a business?

A revolver *accelerates* cash flow by enabling a business to borrow against the future value of receivables and/or inventory that are expected to become cash in the near term. This acceleration of cash provides liquidity and allows the borrower to extend and optimize its equity base.

21. Does my company need to be profitable to use asset based lending?

No, not necessarily. A lack of profitability does not eliminate asset based lending as an option. A company that has experienced a profit downturn may still be eligible provided its management has identified the problem and developed a viable corrective action plan. In addition, many companies which are not profitable have fine operating results and simply need to adjust their capital structure. Asset based lenders can help through a variety of recapitalization approaches including loan restructures, asset spin-offs, and cooperative dispositions.

If bankruptcy is a possibility, borrowers can consider a Debtor-In-Possession (DIP) facility. In such cases, prospective borrowers should inquire as to the lender's experience and expertise regarding financing and the bankruptcy process; not all asset based lenders are knowledgeable about this highly complex arena.

For more information on bankruptcy financing, please see questions beginning on page 27.

22. Can an asset based loan be used to finance an acquisition?

Yes, this is a commonly used means to finance acquisitions. In fact, it is possible to use the *assets of the company being acquired* to finance the acquisition. This can be especially advantageous when the prospective acquisition has a high level of eligible receivables and/or inventory in relation to the purchase price of the company. Such companies are often excellent prospects for acquisition, and asset based lending can provide a significant source of the acquisition capital.

23. Can asset based lending be used as growth financing?

Yes. A revolving credit facility will tend to give a business the greatest amount of flexibility and borrowing capacity from its existing asset base. An innovative asset based lender can design a facility that can grow as the company grows. For example, a revolving credit facility could be designed to provide a higher credit limit as the business increases its borrowing base, provided certain key operating ratios are maintained. As the company's needs and collateral grow, so can its ability to borrow.

24. What are covenants? What covenants are customary for an asset based loan?

Covenants are simply promises to conform to specific guidelines as part of a loan agreement. They are customary for asset based loans. An example of a covenant would be the borrower's promise to conform to specified financial ratios for the life of the loan. Covenants help the lender monitor and control the loan while providing the borrower with the greatest possible loan.

25. Is a "zero covenant" loan a good deal?

Maybe. Covenants are "tools of the trade" that help the lender monitor the loan's performance. For example, if a lender provides an asset based loan with no covenants, the lender may have to structure the deal as a demand loan to protect its interests. Then, if the borrower's financial condition deteriorates markedly, the lender may decide to cut off cash availability to the borrower and terminate the loan without notice. In contrast, a loan including performance covenants can give the lender some latitude to work with the borrower in such a situation, to the benefit of both parties.

26. What confirmation procedures are customary in an asset based loan?

A lender customarily confirms financial and collateral information provided by the borrower in order to support ongoing loan requests. There are two basic types of confirmation:

(a) Field Examinations. Many major lending organizations have a field examination group that visits the borrower's operation to better understand its business. *Field examinations benefit the borrower because they enable the lender to provide the maximum amount of liquidity possible which can be supported by the collateral*. A field examination is not like the audit a CPA firm would conduct at a business. Instead, it confirms collateral and financial information and helps the lender evaluate trends in the borrower's business. Although transaction costs can be structured in a vast variety of ways, in most cases the prospective borrower is responsible for costs related to a field examination.

(b) Accounts Receivable Verifications. Verifying accounts receivable simply involves confirming some or all of the borrower's receivables directly with the borrower's customers.

27. What is factoring?

In a traditional factoring arrangement, a company actually sells its receivables to another company (a "factor") at a discount. After the sale, the receivables balances are carried on the factor's balance sheet since title has passed. Because the factor then owns the receivables, it generally provides all the required credit, collection, and accounting services necessary to collect the receivables, including assumption of the ultimate loss exposure from the client debtor.

The important difference between factoring and asset based lending is ownership. In factoring, the receivables are purchased and owned by the factor. In asset based lending arrangements, accounts receivable are pledged to the lender as security for the loan, but the borrower retains ownership and complete control of the receivables and the value of the receivables remains on the borrower's financial statement.

28. When would a company use factoring?

In some industries, including textile and apparel manufacturing, the use of factoring is very common. Factoring is appropriate if the seller of the receivables (a) seeks to shed its risk and the cost of collecting receivables from its customers, and (b) is willing to allow a third party to have control of a portion of its relationship with its customers. While factoring eliminates the time, expense, and risk related to collecting receivables, it is the factor—*not the company that sells its receivables*—that conducts the payment or collection process with the end-customer.

29. How is "floor plan financing" different from a revolver secured by inventory?

Floor plan financing is a method of financing inventory that usually involves a manufacturer selling its product to a dealer or distributor. While a revolver secured by inventory is designed to help the borrower meet the overall financial needs of a business, floor plan financing typically is geared to the acquisition of specific items of inventory. For example, a tire manufacturer may use a floor planning program on the tires it supplies to a seller of auto parts and accessories. Floor plan financing often takes the form of a purchase money security interest, through which a seller of goods on credit retains a preferred lien on the goods sold to secure payment of the purchase price, or through which a lender who advances funds to enable the borrower to acquire certain goods is granted a preferred lien on the goods so acquired to secure repayment of the funds advanced.

30. Is tax leasing a type of asset based lending?

Tax leasing differs from asset based lending in that the lessor owns the equipment (instead of taking it as security for a loan) and leases it to the end user. As the owner of the equipment, the lessor typically gains all the tax benefits for its own account along with the risk of obsolescence regarding the leased equipment. Both leasing and asset based lending use traditional collateral monitoring techniques to provide the lessee or borrower with the largest possible amount of funding while at the same time minimizing the financier's risk. A lessor that understands the inherent value of the equipment will be able to grant the borrower the most generous amount of funding from a specific asset. Additionally, due to the tax benefits of ownership belonging to the lessor, the effective stream rate on a lease may be lower than the interest rate on a traditional equipment loan. A lease may be structured as off-balance sheet financing. A financing company that can provide both leasing and asset based lending would be best able to evaluate your needs objectively and provide the optimal funding mix.

For more detailed information on equipment leasing, please refer to our booklet "Helping You Through the Leasing Maze," which is available by calling the GE Capital Information Center at 1-800-243-2222.

31. Should I expect an asset based lender to understand the cycles of my industry?

Yes. You are absolutely entitled to expect your lender to understand your business. If you work with a lender that is not fully aware of how your industry's cycles impact your business, you may find your ability to borrow is cut back or even eliminated at exactly the time when your demand for credit is highest. The more your lender knows about your business, the more your lender can do for your business. Expect and demand that your lender know a great deal about your industry from the start, and expect your lender to actively learn more about your industry and your business as the relationship evolves.

32. If a company is in bankruptcy, does that necessarily mean it is not creditworthy?

No. A company in a Chapter 11 bankruptcy proceeding is frequently considered a more creditworthy borrower due to the supervision and protection implicit in a Bankruptcy Court proceeding. Bankruptcy proceedings may occur for many reasons, including: (1) poor capital structure, (2) poor operating results, (3) inability to fully access liquidity, (4) pending litigation, and (5) unfavorable contracts or leases. There are as many reasons as there are companies that go into bankruptcy.

In bankruptcy, pre-petition creditors are prevented from taking action against the debtor. While secured creditors are entitled to adequate protection, unsecured or undersecured creditors are blocked from receiving any payments during the case. An asset based lender providing Debtor-In-Possession (DIP) financing following the filing of either a voluntary or involuntary bankruptcy proceeding utilizes the same fundamental asset valuation approach to provide the loan as it would utilize for a company not in bankruptcy. The availability of DIP financing may depend on the perceived viability of the company during the proceeding and on its ability to successfully complete a Plan of Reorganization (POR) or Section 363 asset sale (these terms are defined in the Glossary).

The availability of capital—and access to it—is the foundation of a company's ability to operate in bankruptcy. It is *absolutely critical* that any company considering a Chapter 11 proceeding contact a prospective lender to determine the availability of DIP financing prior to initiating a proceeding. In most cases, DIP loans are arranged for prior to or in conjunction with the actual petition date.

For more information on bankruptcy, please see the questions beginning on page 27. *For specific advice regarding your needs with respect to bankruptcy, contact a competent restructuring specialist, an attorney specializing in this field, or both*.

33. What is the difference between asset based lending, revolving credit facilities, and commercial finance?

Asset based lending refers to loans secured by a wide variety of assets. Businesses can borrow money using the liquid, current assets of the company (such as accounts receivable and/or inventory) or the fixed assets of a business (such as plant, property, and equipment) as collateral. Asset based lenders rely on the value of the underlying collateral to minimize the loan's credit risk. Asset based loans also can include equipment loans and real estate mortgages. Commercial finance is the term most commonly affiliated with the industry group of lenders that provides all types of asset based loans to business and commercial borrowers. Asset based lenders are sometimes referred to as secured lenders.

34. How does a finance company differ from a bank?

While both lend money to businesses, a bank's lending activity and reserve requirements are regulated by state and federal governments. Finance companies are not regulated in the same way and, as a result, can take on a wider variety of loans and move faster in response to market changes and customer needs. Some finance companies are part of large manufacturing and/or distribution concerns and were originally created to provide financing for customers. Such lenders can provide unique practical insight into business borrowing needs.

35. What is risk rating of loans? Do all lenders engage in risk rating of loans?

Not all lenders risk rate their loans. A lender that is not subject to state and federal bank regulations is not required to risk rate its loans. However, lenders who accept public deposits, such as commercial banks that also provide asset based loans, must risk rate their loans for the respective state and/or federal bank regulatory agencies. Unfortunately, no one particular standard has been accepted by all lenders and/or regulatory agencies. As a result, the explanations of exactly how an institution rates its loans will vary widely. Many different scales are used so the actual number (or "score") used to rate a borrower's loan may provide little useful information.

36. Can risk rating of loans have a significant impact on a borrower?

Yes, it can. Factors outside of a bank's control have the potential to change the way its asset based lending accounts are handled. For example, should there be a downturn in a specific industry or geographic area where the bank has loan activity, bank regulators may look at the institution's underwriting criteria and their portfolio of like businesses and require the bank to post new and higher loss reserves, or stop accruing interest on similar asset based lending accounts. That can result in an account being transferred to a bank work-out group that is more closely supervised by the bank regulators. The net effect on the borrower could be as significant as being asked to find a new lender, a process that can substantially disrupt the borrower's day-to-day operations. Depending on the performance of the borrower's business at that time, having to find a new lender may be extremely difficult and costly. Factors outside a borrower's control but *within* a bank's control, such as a bank's decision to make more volatile loans for real estate ventures or third world debt, also can have an impact on a borrower.

37. What is more important in selecting a lender: the people or the institution?

An argument could be made that the people *are* the institution when it comes to lending money. A good working relationship with your lender is important because you will be interacting regularly, in all likelihood every day. Make sure you are comfortable with the people *and* the organization. Are the people you propose to work with innovative and knowledgeable? Are they part of an organization that is committed to asset based lending? If your lender does not have a specific product to suit your needs, will it be able to create one for you? As your business grows and changes, will your lender have the resources to address your evolving capital needs? Is your lender financially stable? (Its stability is directly related to its ability to raise money and, therefore, to your ability to borrow money.)

38. I'm thinking of an IPO in the next 18 months. How can the selection of an asset based lender impact my company's ability to issue stock?

Lenders, just like businesses in your industry, have reputations for the types of customers they tend to serve. Some lenders specialize in financing distressed companies, others specialize in financing certain industries such as health care companies. Some institutions have more *cachet* value to outside investors than other companies. If you are planning an IPO, the selection of your lender is important because the potential purchasers of your stock will be relying on this lender to supply the company with working capital as it grows. Institutional investors in particular tend to like a recognizable and stable institution for a company's senior lender.

39. Can my law firm represent me in the closing of the loan?

Any law firm which is competent and experienced in matters of financing a business can represent you in the closing. However, a law firm which is competent and knowledgeable about your business in many legal matters may not always be the best choice to represent you in documenting a new asset based loan facility. The *wrong* law firm can cost you significant time and money because of extended negotiations over matters that are common to these types of transactions. This point is particularly true if you are planning an acquisition or are seeking bankruptcy protection and need a DIP facility. Keep in mind, too, that a law firm is a business, and just as your business seeks to make new and incremental sales, so will a law firm.

To ensure you have appropriate representation, ask about the firm's specific experience in asset based lending. Ask for references of companies similar to your own that it has advised on an asset based loan facility, and check the references. If your lawyer does not possess the background to represent you, you may wish to consider retaining a lawyer with the appropriate expertise.

40. Can my in-house counsel represent me in these transactions?

Most companies do not choose their internal counsel to represent them for an asset based loan transaction. Though typically competent and often uniquely knowledgeable about your business, internal counsel generally are not *specialized* in this highly technical field. As a result, they do not possess specific, technical knowledge that is critical in order to represent the legal interests of your business properly and cost-effectively. Additionally, because of their typical work load, internal counsel may not have the time to respond as quickly as necessary to the information requests that asset based lending transactions generate. This can cause delays in closing and funding the transaction. Representing a borrower is a time consuming process requiring an intense level of effort concentrated in a short period of time. As a result, internal counsel often cannot meet both their ongoing commitments and the information requests to support the loan while conducting the loan representation in a timely manner.

41. What kinds of fees are typically involved in an asset based loan?

Fees are generally charged to the borrower to help the lender recover its initial costs in putting a transaction together and to contribute toward earning a fair profit. There is generally a *commitment fee* and *closing fee* for an asset based facility. The commitment fee is paid in cash upon obtaining the commitment. The commitment fee is often credited toward payment of the closing fee, and the balance of the closing fee generally is paid from the proceeds of the initial loan. Each of these fees may range from one-half of 1% of the loan to many times that amount.

Fees may vary depending on the creditworthiness of the borrower, the type of event being financed, and other factors. For example, fees charged to a company that needs a bankruptcy facility will differ from a very successful company that is seeking to conclude a refinancing of its senior loan facility, and from a sponsor group seeking to acquire a business through a leveraged buyout.

Depending on the type of loan, some other typical fees may include: (a) an *unused line fee* which is designed to compensate the lender for its cost to retain the liquidity to lend the borrower the maximum amount of their committed facility as needed, (b) an *administrative fee* to compensate the lender for ongoing collateral auditing and monitoring, (c) a *prepayment fee* to compensate the lender if the borrower decides to end the facility (and the lender's projected income from the loan) prematurely, and (d) an *audit* fee. Not every borrower pays every fee.

Other costs which are the borrower's responsibility include the field examination and the borrower's and the lender's legal representation. The amount of these fees will vary according to each borrower's circumstances.

42. How long does it take to close a revolving credit facility?

Normally you should expect a 4 - 6 week period from the date a proposal is accepted until a new facility is funded. Of course depending on the complexity, type of facility, and amount of negotiation engaged in by the parties, it may take more or less time. Certain types of transactions, such as Debtor-In-Possession transactions, are commonly concluded or committed to within a few days. Closing can take longer if unusual circumstances such as significant inter-creditor negotiations or third party consents are required to complete the transaction.

43. How do I close a new facility with the lowest possible cost and in the least possible time?

The cost of closing can be driven up by a number of factors, many of which the customer can control. For example: extensive customer negotiation over terms common to asset based loan contracts; pushing the structural limits of a given type of loan; selecting a lender that makes incrementally more stringent demands; and using a law firm unfamiliar with asset based financing.

The following suggestions can help speed the process and minimize cost:

(a) *Be open*. The final decision to lend, and the terms on which a loan is made, will be based in large measure on a thorough analysis of your company. You expedite the process and the lender's decision making by providing complete information regarding your company as soon as appropriate.

(b) *Be knowledgeable*. Every lending relationship is a two-way street: you want to borrow money and a lender wants to lend it to you. Both you and your lender have key responsibilities throughout the lending process. Know your responsibilities and your needs. Know what is practical and possible for your business as well as for a prospective lender.

(c) *Commit.* Understand that the closing process is the foundation of your new lending relationship. Be willing and prepared to commit sufficient time and energy to get the process started and completed in a timely manner.

44. How do commercial lenders earn a fair profit?

The cost structure of a commercial lender such as GE Capital is not unlike that of a manufacturing concern. Where a manufacturer incurs cost of goods sold, we incur interest expense from raising funds in capital markets. Like nearly all businesses, we also incur overhead expenses such as salaries, operations, insurance, etc. Where a manufacturer earns income by selling its goods, we earn income by charging interest on the money we lend. A portion of our income comes from fees charged to the borrower to help us recover our initial costs in putting a transaction together and to contribute toward earning a fair profit.

GE Capital raises funds for lending in the commercial paper markets. In fact, GE Capital is the world's largest issuer of commercial paper and has earned the highest credit rating (AAA) by both Moody's Investors Services and Standard & Poor's.

45. How does GE Capital price loans?

GE Capital prices loans in order to provide cost-effective capital for our customers while earning us a fair profit. Most loans that we underwrite and fund are "floating rate loans" which means that the interest rate charged to the borrower may go up or down based on an index such as LIBOR, CP or the Prime Rate. These indexes are described below:

- LIBOR (London Interbank Offered Rate) is the rate that the most creditworthy international banks, dealing in Eurodollars, charge each other for large loans.
- CP (Commercial Paper Rate) is the rate associated with high quality corporate short-term negotiable notes having an original maturity of less than 270 days.
- The Prime Rate is determined by banks after considering many economic factors including the Federal Reserve's decision to raise or lower prevailing federal funds interest rates for banks' short-term borrowings. Banks use the Prime Rate in pricing commercial loans to their best and most creditworthy customers.

The interest rate on GE Capital loans is generally based on LIBOR rates plus a spread. The spread varies according to each client's creditworthiness and circumstances. Although interest rates change as the market changes, borrowers can control their expense with rate caps, floors, and collars.

Changing economic conditions and new options for financing have combined to provide vast opportunities—and potentially serious consequences. The emergence of a robust junk bond market during the late 1980's led to a significant number of over-leveraged companies. Leverage enhanced the success of many such companies. But the economic recession of the early 1990's introduced change, and many over-leveraged companies found themselves unable to service their debt and facing bankruptcy.

Among lenders that emerged to provide innovative bankruptcy financing, GE Capital is widely viewed as a leader. Based on our knowledge of bankruptcy financing and our experience using change to our customers' advantage, we have provided answers to commonly asked questions about bankruptcy financing. The information that follows is intended to introduce you to bankruptcy lending. It is not intended to provide legal advice. Before filing a bankruptcy petition, it is crucial that you seek the advice of competent, experienced legal counsel.

46. What is bankruptcy?

When your company runs out of cash or incurs an unusual liability, bankruptcy gives you a legal safe harbor to let you reorganize. Bankruptcy is a legal strategy that provides relief from creditors while a company deals with a liquidity crisis or recapitalizes to reduce leverage. Bankruptcy law governs a wide range of activities including business liquidation, but it should not be viewed solely as a means of liquidating a failed business. More often, it is used as a tool to reorganize or restructure a business to once again operate profitably. In all cases, bankruptcy law attempts to protect the rights of both the debtor and its creditors.

47. Why would a company consider filing bankruptcy?

There are many reasons companies file bankruptcy petitions, but the four most common are:

(a) The company is experiencing continuing operating losses;

(b) The company has leases or executory contracts that contribute to continuing operating losses and files in order to terminate the leases or contracts;

(c) The company is experiencing liquidity problems resulting from a lack of cash or from the inability to refinance, on acceptable terms, long-term debt obligations coming due; and

(d) The company has significant long-term obligations which have emerged from product liability claims (such as asbestos related claims) or extraordinary judgments (such as EPA Superfund obligations).

48. Are there different kinds of bankruptcy filings?

Yes. A company experiencing continuing operating losses, liquidity problems, or long-term obligations would generally file for protection under Chapter 11 of the Bankruptcy Code while it reorganizes and gets back on its feet.

A company that expects to go out of business might file bankruptcy under Chapter 7 to provide for an orderly liquidation of its assets. Municipalities file under Chapter 9, family farmers under Chapter 12, and individuals under Chapter 7 or 13.

49. Who decides whether a company files bankruptcy?

A bankruptcy filing can be either voluntary or involuntary. The difference is essentially whether you elect to file your bankruptcy petition (voluntary) or someone else files a petition to force you into bankruptcy (involuntary). Filing voluntarily lets a company choose where the legal proceedings take place and can provide the company with more control over its situation. If a company is forced into bankruptcy by its creditors, the creditors could choose to start legal proceedings in a location that may not be convenient to the company. That could require a special trip to court for the company to request a more convenient location, which may or may not be granted. Always remember that creditors have rights; a company cannot be cavalier in deciding not to pay its creditors. A debtor will rarely be offered refuge under bankruptcy law when the debtor can pay debts rightfully owed without undue hardship.

50. Does a company have to be insolvent to declare bankruptcy?

A company is usually considered to be insolvent when it is unable to meet its debts as they come due, has too little capital to operate properly, or has debts which exceed the value of its assets. A company usually faces one of these conditions when it is considering bankruptcy, but a debtor does not have to be insolvent to file bankruptcy.

51. Is it possible to borrow money in bankruptcy?

Yes, with bankruptcy court approval. A Debtor-In-Possession (DIP) may obtain unsecured financing that has priority over all unsecured claims. If a DIP is not able to obtain unsecured financing, it can seek approval for a secured loan.

52. Who can provide a DIP loan?

It is critical that a lender providing a DIP loan have specialized experience in both asset based lending and bankruptcy financing because a DIP loan requires the approval of the Bankruptcy Court and usually involves a pledge of collateral. A company in bankruptcy cannot properly borrow substantial sums without court approval.

53. Does your current lender have to provide your DIP loan?

No. In fact, you may have difficulty getting your current lender to provide a loan if it has developed “lender’s fatigue”—the industry term used to describe a lender’s unwillingness to continue a troubled lending relationship.

It is often possible to get a DIP loan from a new lender provided that the DIP has unencumbered assets to secure the DIP loan or is able to grant a “priming lien” on encumbered assets by providing “adequate protection” of the interest of the existing lender holding a lien on such assets. A creditor’s interest may be adequately protected when its collateral is valued sufficiently in excess of the obligations owing to it.

54. What is a Plan of Reorganization?

A plan of reorganization (POR) is the document which outlines the Chapter 11 exit strategy of the DIP. It sets forth the new capital structure of the DIP and the treatment of the various classes of creditors and equity holders. The POR must be confirmed by the bankruptcy court before it can become effective. The DIP has the exclusive right to propose a plan within the first 120 days of the Chapter 11 case, subject to extension by the court.

A DIP usually tries to negotiate a consensual POR with its major creditors. Each class of creditors will be entitled to vote on a POR. If it meets all the requirements of the bankruptcy code, a POR will be approved if it is accepted by each class of the DIP's creditors and equity holders (generally a 2/3 majority). A POR may be "crammed down" and confirmed over the objections of a class of creditors or equity holders if it does not discriminate unfairly and is fair and equitable (conforms to the "absolute priority rule"). Once confirmed, the plan is binding. Specialized financing is often an integral part of a POR and may be critical to a company's successful emergence from bankruptcy.

55. How important is selecting the right legal representation for bankruptcy?

Vitally important. Seek out competent, specialized counsel before filing bankruptcy. Bankruptcy is a very highly specialized and technical branch of the law, and an experienced practitioner can greatly smooth a company's path through the process. An attorney who sits on your board or your internal counsel is probably not the right person to represent you, but he or she may be able to help you locate and evaluate law firms that practice bankruptcy law.

56. How can filing bankruptcy make a reorganization possible?

Filing a bankruptcy petition gives you time to work out a plan to reorganize the business. When you file a bankruptcy petition, you can often stop paying your prepetition creditors, but you still will need cash flow to continue operating in bankruptcy. Cash enables you to pay employees and post-petition trade creditors while you reorganize the company to emerge with a plan for a fundamentally profitable business. You could generate cash from operations while in bankruptcy. You could borrow it provided you can obtain DIP financing. In some circumstances you could raise cash by selling assets. How you create cash flow will depend on your situation, but you must have it to make bankruptcy successful.

57. If a pre-petition loan is paid off using bankruptcy financing, is the debtor liable for the prepayment penalty?

Filing bankruptcy is a default under a company's loan agreements, which generally means the loan immediately comes due. To determine whether or not a prepayment penalty must be paid, seek advice of competent bankruptcy counsel to review your loan agreement and to advise you as to the practice in your bankruptcy court. Regardless, under such circumstances a company considering bankruptcy should carefully weigh the decision of which lender to bring in for bankruptcy financing.

58. What happens to a negative pledge agreement if the company files bankruptcy?

A company that has an unsecured working capital line may have made a negative pledge agreement whereby it promises not to secure certain assets such as inventory or receivables to any other lenders. However, once the company files bankruptcy it is protected from lawsuits brought by its prior creditors, so a negative pledge would no longer be enforceable by a prepetition lender. In securing bankruptcy financing, a company can generally secure whatever assets are unencumbered.

59. If a lender will give a company financing going into bankruptcy, does that mean it will guarantee to provide financing to emerge from bankruptcy?

No. Expect a lender to make two separate credit evaluations—one to finance your business on entering bankruptcy and another to finance it as it emerges.

60. What is a preference payment?

A preference payment is a payment or transfer of property (including the transfer of a security interest) not in the ordinary course of business to or for the benefit of a creditor made within 90 days (or one year in the case of a creditor who is an insider) of bankruptcy on account of antecedent debt. Payments to a fully secured creditor are not preferential because a transfer is only a preference if it allows a creditor to receive more than it would receive in a Chapter 7 liquidation. The preference rules are designed to prevent a race by creditors to seize a debtor's assets on the eve of bankruptcy and to ensure an equitable distribution of the debtor's assets. A DIP or trustee may seek the return of preferential transfers for the benefit of all of the estate's creditors.

61. How can a company pay lenders or lawyers to perform due diligence if it is in dire straits?

It is possible to pay for these costs out of the money that is available in the ordinary course of business prior to filing. Once a company files bankruptcy, however, it cannot pay attorney fees or lender fees without court approval.

62. What costs are involved in bankruptcy?

Bankruptcy is expensive. There are significant costs which may include legal fees or retainers, the expenses of court-appointed committees and professionals, court fees, a lender's due diligence and loan fees, investment bank fees if new stock is issued, and development of a plan to emerge from bankruptcy. While circumstances may allow trade suppliers to continue shipping goods once bankruptcy is filed, some customers may turn to a competitor who is not in bankruptcy. In addition to out-ofpocket expenses, management must also weigh the impact bankruptcy will have on its business operations. The process disrupts the normal conduct of business. Opportunity costs, which may be difficult to measure, are very much an element of bankruptcy.

63. What are "prepackaged" bankruptcy and "prearranged" bankruptcy?

Both involve planning the POR before filing. In a prepackaged bankruptcy, the company, lenders, and the trade usually have formally agreed to the deal in advance. In a prearranged bankruptcy, the company works out details up front but has not had or concluded formal discussions with lenders and has less assurance the trade suppliers or trade creditors and other lenders will go along.

Glossary of Commonly Used Terms

This glossary is intended to help you understand the meaning of terms commonly used in asset based lending. When a defined term is followed by a term in parentheses, the two terms have essentially the same meaning. Many of the terms defined are used within this guide. Some terms defined in the glossary are not used elsewhere in the guide, but since you may encounter these terms in the asset based lending industry, we have included them for your reference.

[A]

Account
An account receivable or an open account. In the commercial finance industry, "account" refers to an indebtedness; the person or company owning the indebtedness is an "account debtor."

Account Debtor (Debtor)
A customer billed by a client for a product shipped or service rendered.

Accounts Receivable Credits (Dilution)
Returns, allowances, discounts, or other offsets to accounts receivable.

Accounts Receivable Debit
An increase to accounts receivable. A debit may be the result of sales, interest charges, freight charges, or collection costs.

Acquisition Financing
A loan to a business, entrepreneur, or equity sponsor group to assist in acquiring the stock or assets of a business. Sometimes referred to as a "bootstrap" loan or a "buyout" loan.

Advance Rate

The percentage of funds extended to a client against eligible collateral as stated in a lending contract. Example: A client with a contractual advance rate of 80% assigns as collateral invoices totaling $100,000. The client receives a loan of $80,000 at once, and upon collection of the invoices, receives the balance of $20,000, on a day-to-day basis as collections are received, less any dilution.

Aging

A schedule of accounts broken down according to the month of an invoice's original billing date.

Airball

The portion of an asset based loan which is not covered by collateral.

Appraisal

The valuation for collateral purposes of property, such as equipment or inventory, against which a loan is to be made.

Assignment of Accounts Receivable (Report of Assigned Accounts)

An instrument wherein a client assigns, reports or pledges receivables to the lender to secure a loan.

Assignment Jacket

A pouch containing all bills and receipts that a borrower assigns to a secured lender.

Availability

The amount of money a client has available to borrow, determined by the sum of collateral values less all ineligibles, multiplied by the agreed advance rate.

Average Collection Period (Turnover)

The average number of days in which cash receipts will liquidate receivables.

[B]

Bill and Hold

Merchandise billed to an account debtor but not shipped. The merchandise may be marked as property of the debtor and is held pending shipping instructions.

Blind Endorsement

Endorsement of checks collected by clients in favor of the lender by means of a number or symbol, so that the lender's name does not appear.

Borrower's Fatigue

A strained lending relationship that occurs when the borrower tires of a lender, typically for refusing to modify its loan agreement to reflect the borrower's improved financial condition.

Borrowing Base Certificate

A form prepared by the borrower that reflects the current status of the collateral. Borrowing base certificates may be due on a daily, weekly, or monthly basis.

Bulk Handling

Managing information obtained from reporting, accounting records, or aging prepared by client, but with no detail of account debtors.

C

[C]

Circled

A transaction is said to be hard circled" when all issues are resolved and participants are committed. Verbal agreement may constitute a soft circle.

Clearance

Average number of days necessary for deposited checks to pass through a clearing house (decided by contract, usually 3 to 5 days).

Client

The borrower.

Collection Report (Remittance Report)

Form used by client to itemize collections sent to the lender each day.

Collateral

Security offered by a client to obtain a loan. Collateral may include inventory, accounts receivable, equipment, securities, real estate, or certain other assets.

Commensurate Balances (Compensating Balances)

Funds that a borrower is required to keep on deposit with a bank extending a loan.

Commercial Financing

Various types of asset based financial services in which money is loaned by a secured party to a debtor, pursuant to a loan and security agreement which gives the lender a security interest in specified types or items of collateral. Note that commercial financing is different from factoring. In commercial financing, the secured party is entitled in all events to be repaid the money loaned. In accounts receivable factoring, the secured party (the factor) takes a loss if a factored invoice is not collected due to insolvency. If the account debtor becomes insolvent, the factor assumes the credit risk on that particular account debtor or invoice.

Commitment Fee

A fee from a lending institution as consideration for its undertaking to make a loan to a prospective borrower, charged when the borrower meets the preconditions specified in the commitment. Depending on the terms of the deal, a commitment fee may be non-refundable or it may be credited upon closing the loan.

Concentration (Jumbo Account) Ratio

The percentage of total receivables billed to single debtor.

Consignment Sale

A sale of merchandise to a buyer by a middleman in which title passes directly from the owner to the buyer. The owner expects payment only on completed sales, and unsold items may be returned by the middleman to the owner.

Contra

An account created when a company both buys from and sells to the same client and, therefore, has payables and receivables which offset.

Conversion

A client's unauthorized deposit of collections of accounts assigned to a lender.

Credit Insurance

A policy held by a client which protects the client against losses due to bad debts.

Cross Aging

When past due receivables exceed a given percentage of a debtor's total accounts receivable, the current portion of receivables is also classified as ineligible.

D

[D]

Datings

Terms of sale which extend the period within which the debtor is to make payment. Example: Normal terms are Net 30 Days. On a bill for merchandise shipped September 15, a bill is dated "as of November 15" making payment due December 15.

Debtor-In-Possession (DIP)

A business entity which is the subject of a reorganization proceeding under Chapter 11 of the Bankruptcy Code. Unless and until a trustee is appointed, the Debtor-In-Possession operates its business and has all the powers of a trustee to manage the affairs of the business and administer the case.

Demand Loan

A demand loan is repayable on demand rather than on a specified date. In practice, demand for repayment is not generally made unless the borrower's condition deteriorates so much that the lender concludes its risk has become too great to continue the existing account.

Detailing (Ledgering)

The posting of all transactions of a client's pledged accounts receivable to the records maintained by the lender. Detailing should agree with client's subsidiary ledger at each periodic examination.

Dilution (Credit)

Returns, allowances, credit losses, discounts and other offsets against accounts receivable. Dilution drives the advance rate in a transaction.

DIP Financing

Financing extended to a Debtor-In-Possession under Chapter 11 of the Bankruptcy Code. In most cases, DIP financing is considered attractive because it is done only under order of the Bankruptcy Court, which is empowered by the Bankruptcy Code to afford the lender a lien on property of the bankruptcy estate and/or a priority position.

Double Assignment

The assignment of receivables by a subsidiary, parent, or other affiliated company to the borrower, which in turn assigns the receivables to the lender.

E

[E]

Eligible Accounts

Sometimes called "acceptable accounts" or "prime accounts." These are receivables which satisfy the criteria specified in the security agreement so that they are acceptable to the secured party and included in the borrowing base as eligible collateral and entitle the debtor to an advance. Receivables which do not meet the criteria are called "ineligible."

Equity

The percentage due from lender to client upon collection of bill, calculated as the amount collected less the contracted advance.

Excess Availability

Total availability less the aggregate advances made on the outstanding revolving loan.

F

[F]

Field Audit (Field Examination)

An examination and inspection of a client's books, records, property, and operations, with particular attention being paid to the condition of the collateral. In revolving financing on receivables or inventory, regular field audits are an essential feature of the secured party's monitoring.

Filing

In the UCC context, filing is the act of depositing in a public office a document, usually a financing statement, which gives legal notice of the secured financing transaction. In most secured transactions, filing is an essential step in the process of perfecting the security interest.

Financing Statement

Generally known as "Form UCC-1." This form is filed in the prescribed public offices for the purpose of perfecting the security interest of a secured party.

[G]

G

Guaranteed Sales

Sales of merchandise for which payment is made in normal course, but with the understanding that unsold merchandise may be returned for a full refund. Title passes to the debtor.

Grid Loan

A secured but not heavily monitored loan. As long as the borrower's company performs according to the loan agreement, collateral monitoring is minimal.

Guaranty

A document by which a person or corporation (a "guarantor" or "surety") promises payment of a debtor's obligations to a secured party. It is quite customary to require guaranties from the principals of a debtor and from the debtor's parent, subsidiary, or affiliates.

[H]

H

Haircut

When a lender wants to end a transaction in advance, it often will accept a reduction in principal or interest accrued (i.e., a haircut) in order to be paid out in cash.

High Debtor

A debtor whose balance represents 5% or more of a company's total receivables (see Concentration).

Holdback (Reserve)

The balance of an invoice in excess of the advance. The holdback becomes equity when the invoice is paid.

I

[I]

Ineligible (Non-Prime)

Invoices assigned to the lender, against which no advance is made. Ineligible invoices may be past due according to contractual terms (90 to 120 days from invoice date), contra, employees, affiliates, consignments, memo guaranteed sales, or in excess of limit allowed to the debtor.

Initial Assignment (Original Accounts Receivable; Report of Assigned Accounts)

Instruments used to convey an interest in accounts receivable to the lender in order to secure the initial advance.

Insolvency

Technically, the financial condition of an enterprise whose liabilities exceed its assets, or which is unable to pay its debts as they mature. Financing an insolvent client requires specialized lending expertise, particularly if insolvency leads to bankruptcy. Bankruptcy tends to be the path followed by insolvent companies, but it may actually open up alternative financing opportunities.

Inventory Financing

Sometimes called "inventory loans." Advances made to enable a client to acquire, manufacture, or carry inventory. They are collateralized by a security interest in the inventory and usually in the accounts receivable or other proceeds of sale.

Involuntary Bankruptcy Filing

An involuntary bankruptcy filing occurs when a creditor or group of creditors forces a company into bankruptcy. This may severely restrict the ability of the bankrupt company to control its own situation.

[J]

J

Jumbo Account (Concentration)

A debtor having a balance in excess of 5% of a company's total receivables.

[L]

L

Landlord's Lien

The privilege given by some state statutes to a landlord when a tenant has not paid rent due which allows the landlord to impose a lien for the rent against the tenant's property located in the leased premises. Since the landlord's lien is a potential rival to the UCC security interest, secured lenders often try to obtain a landlord's waiver in advance, before taking on a prospect in a state which recognizes the landlord's lien.

Ledgering (Detailing)

The posting of all transactions to reports maintained by lender of a client's accounts receivable assigned to the lender. Ledgering should agree with the client's subsidiary ledger at each periodic examination.

Lender's Fatigue

Occurs when a borrower continually disappoints the lender by missing financial targets or failing to live up to terms of the contract. In such circumstances, the lender may, depending upon its rights under the contract, ask or require the borrower to refinance.

Letter of Credit

An undertaking by a bank that, upon the presentation to it of specified documents, it will pay a specified amount to the presenter. Letters of credit are used traditionally in international transactions to assure that a shipper of goods will be paid for them.

Line of Credit

A commitment, by a bank or other lender, to lend money to a borrower up to a maximum amount during a stated period.

[N]

Negative Pledge

A promise not to secure certain assets of a company, such as inventory or receivables.

Non-Prime (Ineligible)

Invoices assigned to the lender, against which no advance is made. Ineligible invoices may be past due according to contractual terms (90 to 120 days from invoice date), contra, employees, affiliates, consignments, memo guaranteed sales, or in excess of limit allowed to the debtor.

[O]

O

On-Account Payments

Partial payments by a debtor which does not pay a bill or bills in full.

Original Assignment (Initial Accounts Receivable; Report of Assigned Accounts)

Instruments used to convey an interest in accounts receivable to the lender in order to secure the initial advance.

Over Advance

A lender's unsecured position that occurs when funds are advanced in excess of contracted terms. Example: Where a stipulated advance is 80% and client is extended 85%, the extra 5% is considered an over advance.

[P]

P

Pack and Hold

Merchandise that is packed and held in inventory against orders. Billing does not occur until merchandise is shipped.

Participation

Occurs when portions of a loan, usually up to 50%, are shared by different lenders.

Pay Statement

A statement that accompanies a debtor's check and which indicates an item or items being paid as well as any existing dilution.

Plan of Reorganization

The document which outlines the Chapter 11 exit strategy of the Debtor-In-Possession. It sets forth the new capital structure of the DIP and the treatment of the various classes of creditors and equity holders. The POR must be confirmed by the bankruptcy court before it can become effective. The DIP has the exclusive right to propose a plan within the first 120 days of the Chapter 11 case, subject to extension by the court. Specialized financing is often an integral part of a POR and may be critical to a company's successful emergence from bankruptcy.

Post-Dated Check

A check drawn in payment of bills, but with the date on the check being some time in the future.

Pre-Billing

Billing by a client in advance of shipping.

Prime (Eligible)

Invoices assigned to the lender, against which advances are made.

Primed

A lender is primed when it has lost its collateral position and moves down in the capital structure.

Progress Billing

Billing made on a percentage of completion basis and generally found in service, construction, and other industries.

Purchase Money Security Interest

A security interest which attaches to specific property in connection with a debtor's acquisition of the property.

[R]

Re-Assignment (Double Assignment)

The assignment of receivables by a subsidiary or affiliate to a parent company, which in turn assigns the receivables to the lender.

Remittance Report (Collection Report)

Forms used by client to itemize collections sent to the lender each day.

Re-Purchase Period

The period of time, generally 90 to 120 days beyond invoice date, beyond which a sale becomes ineligible for assignment in accordance with contract terms.

Reserve (Holdback)

The balance of an invoice in excess of the advance. The reserve becomes equity when the invoice is paid.

Retention (Retainage)

The percentage held back by a debtor on a service contract to ensure adequate performance.

Revolving Credit

A series of loans, secured or unsecured, on which the amount outstanding varies from time to time. Secured financing on receivables or inventory is called revolving because the collateral and the outstanding advances change continually.

[S]

Schedule of Accounts Receivable (Report of Assigned Accounts)

An instrument by which a client assigns, reports, or pledges receivables to the lender as security for a loan.

Security Agreement

The agreement between a secured party and a debtor, providing for asset based financial services and creating a security interest. Many security agreements have identifying captions (e.g., accounts receivable financing contract, inventory loan agreement, trust receipt contract, pledge, equipment lease, etc.). The UCC lumps all of these under the category of security agreement.

Security Interest

An interest in, or lien upon, collateral which secures payment or performance of an obligation. The term includes the interest of a factor who purchases accounts receivable.

Shipping Evidence

A properly executed receipt by a carrier or debtor.

Single Risk Insurance

A policy obtained by a client to cover either one debtor or one invoice against loss.

Skip (Skipped Invoice)

The payment of an invoice by a debtor which leaves the prior invoice unpaid.

Statement

A monthly itemization of all transactions during the month. A statement may be prepared by the lender or by a client for the account debtor.

Sub-limit

A facility with a total advance limit may also specify a sub-limit on maximum loan advances supported by certain types of collateral (e.g., inventory).

Subordination

An agreement or arrangement regarding two obligations owed by a debtor. When the two obligations would otherwise be of equal rank, the agreement or arrangement gives one obligation priority in payment over the other obligation, which is subordinated.

Suppressed Availability

Suppressed availability occurs when a facility has collateral to support a loan advance but the credit line or a sub-limit prevents the borrower from drawing further loans utilizing this collateral.

[T]

T/A (Trade Acceptance)

A negotiable instrument for the amount of a specific purchase and bearing debtor's promise to pay.

Term Loan

A loan, secured or unsecured, with a maturity usually exceeding one year. On the borrower's financial statement, the portion (if any) of a term loan maturing within one year from the date of the statement is shown as a current liability, and the balance as long-term debt.

Termination Statement

A form, generally known as Form UCC-3, signed by a secured party and filed to terminate the effectiveness of a previously filed financing statement. A secured party is required to sign a termination statement after the secured obligation is paid, in order to clear the record.

Third Party Checks

Checks received by a client from a debtor which are payable to the debtor and endorsed to the client.

363 Asset Sale

The ability of a company to secure bankruptcy financing may be affected by whether it can raise cash by selling assets in accordance with Section 363(a) of the Bankruptcy Code. Section 363(a) allows a debtor in bankruptcy to use or sell all noncash property in the ordinary course of its business without prior court approval. Use or sale of such property outside the ordinary course of business requires court approval.

Trade Creditors

Business concerns to which a client is indebted for purchases of goods or services. Since trade creditors are usually unsecured, they provide financing that is a critical part of the capital structure of many companies. If a client experiences financial trouble, maintaining the support of trade creditors can be crucial in developing a workable financing solution.

Turnover (Average Collection Period)

The average number of days in which cash receipts will liquidate receivables.

U

[U]

UCC

The Uniform Commercial Code, in particular Article 9 which covers secured transactions.

UCC Search

A report from a filing officer, obtainable for a fee, that shows what financing statements are on file against a named person or organization. The form of request for such information is widely know as Form UCC-11. Often, one of the first steps taken by a lender or factor when considering a prospect is to obtain a UCC search.

Unsecured Loan

A loan which is not secured by collateral. Unsecured loans are rarely made by commercial lenders.

[V]

V

Verification

A method used to determine the validity of receivables pledged as collateral. Generally a mail or telephone request to the debtor confirms the balance on ledgers.

Voluntary Bankruptcy Filing

Voluntarily filing occurs when a company files a bankruptcy petition before it is forced into bankruptcy by the legal action of creditors. Voluntary filing lets a company choose where the legal proceedings take place and can provide the company with more control over its situation.

[W]

W

Working Capital

Current assets less current liabilities. A company's working capital ratio (also called the current ratio) equals the value of current assets divided by current liabilities. A ratio of 2:1 or higher generally indicates a comfortably liquid working capital position.

GE Capital Resources

GE Capital has come a long way since our business began in 1932 with the single purpose of providing consumer financing for GE appliance sales. Now GE Capital is a major services business of GE, accounting for more than 40% of the income of our parent company and meeting the financial needs of consumers and small, medium, and large businesses better than anyone else.

Value, Service and Productivity

GE Capital succeeds—and helps our customers succeed—by embracing the concepts of value, service, and productivity. Value means developing and delivering products and services with a clear benefit to the customer. Service means responding to customer needs with flexible, creative, and timely solutions. Productivity permits our products and services to be delivered at the lowest possible costs, which helps our customers to become more productive in their own businesses.

GE Capital

The financing activities of GE Capital span the world through our highly focused niche businesses. Our products and services, such as asset based financing, equipment leasing, and loan servicing, give our customers a competitive advantage through greater financial and operating flexibility. We can help you cross borders, grow globally, and profit from change.

With more than 65 years of experience, one of the strongest capital positions worldwide, and AAA credit ratings, we provide the capital and value-added services that give our customers the edge they need in today's global marketplace.

GE Capital Resources

The businesses of GE Capital

Specialized & Mid-Market Financing

GE Capital Commercial Finance (CF) is a leading global provider of innovative financing solutions primarily for leveraged companies. Services include lines of credit, factoring, asset securitization, trade finance, plan of reorganizations, acquisition financing, term debt, preferred and common equity. Our expertise in developing a customized business financing plan can help you maximize the value of your assets and allow you to operate your company with the flexibility you need. GE Capital, with over $300 billion in assets, is one of America's AAA rated diversified financial institutions.

With regional offices in over 30 cities worldwide and a network of over 500 finance professionals, Commercial Finance delivers the innovative financing solutions clients need to manage and grow a business. CF's expertise is in developing customized and flexible credit facilities for our customers. CF delivers its services through customer focused (business) segments: The **Middle Market Group** offers our broad range of credit solutions directly to companies with revenues of $50 million to over $200 million in the United States, Canada, Australia, and Mexico. For smaller enterprises in the United States, CF provides asset-based and receivables management solutions through **First Factors**, **Business Credit** and **Commercial Funding**. CF also has industry-focused groups serving healthcare, retail, and communication companies. In Europe, **GE Capital Finance** is a provider of receivables financing and asset-based credit facilities. The **Merchant Banking Group** delivers financing solutions to buyout and private equity firms, and may also invest directly or co-invest alongside equity sponsor groups.

Commercial Finance is uniquely structured to offer fast, innovative solutions to customers' needs. Because GE Capital is not a bank, CF is not bound by capital adequacy requirements and strict banking regulations. Our professionals approach business as business people, not as bankers, allowing them to take a broader view of risk assessment and asset valuation.

Commercial Finance originators and underwriters work together in the field as a team to streamline the underwriting process, enabling them to adapt more quickly to shifting corporate borrowing needs. This team approach empowers originators and underwriters to make rapid decisions to meet client demands and take full advantage of business opportunities.

When your funding relationship really matters to your business plan, call GE Capital.

Commercial Finance is your conduit to the other businesses of GE Capital— businesses with the products, services, and knowledge to help you finance change and grow. For more information, visit our website at:**http://www.gecommercialfinance.com**.

Commercial Equipment Financing (CEF) provides innovative solutions to the ever-changing equipment financing and asset management needs of growing companies around the world. Through government-guaranteed Small Business Administration loans, direct source tax-exempt financing programs and a wide variety of lease, loan, and sale-leaseback offerings, CEF provides companies with low-cost alternatives to cash as well as expertise in debt, tax, and balance sheet management.

Equity Capital Group (ECG) is one of the leading providers of private equity on a global basis. ECG provides growth capital, replacement or secondary capital, buy outs and buy ins of companies seeking to benefit from the strategic resources and experience of the General Electric Company. It typically takes minority stakes in established private companies, with selected investment in publicly traded companies. The Group invests approximately $5 million to $50 million with innovative and flexible deal structures including convertible debt, redeemable preferred, convertible preferred and common stock. The Group's portfolio is diversified, with investments in the healthcare, insurance, retail, consumer products, transportation and logistics, financial services, media and entertainment, telecommunications, information technology, and industrial products sectors.

European Equipment Finance (EEF) is one of Europe's leading diversified equipment leasing businesses, offering financial solutions on a single-country or pan-European basis. EEF covers Europe extensively, including the UK, France, Germany, Italy, Benelux, Ireland, Central Europe, and the Nordic countries. With over 1,400 employees and $5 billion in served assets, EEF's financial strength and customer-focused service initiatives create the tailored sales financing and leasing alliance programs manufacturers, distributors, dealers and end users need. EEF's experienced sales team has diverse market knowledge including, but not limited to, industrial, transportation, information technology, office equipment, agriculture, and telecommunications.

GE Capital Real Estate provides financing and customer services for most general purpose commercial real estate properties. Financing and investment activities for single assets or portfolios include loans, recapitalizations, equity, and selective purchases of loans or properties. Services include asset management, loan servicing, and pension advisory. Transaction size is $1 million to $500 million.

Structured Financial Group (SFG) provides specialized financial products and services to, and acts as an equity investor with clients in the commercial and industrial, energy, communications, and transportation sectors, worldwide. SFG combines industry and technical expertise with significant financial capabilities to address clients' needs across the capital spectrum. Its services include corporate and acquisition finance, project finance (construction and term), and advisory services. Its products involve a broad range of debt and equity instruments, and it has a particular expertise in structured finance and tax-advantaged transactions including leasing and partnership investments. In the past five years, SFG has structured and financed approximately 200 transactions with an aggregate value in excess of $7 billion, and has more than $10 billion in assets. Based in Stamford, CT, SFG has some 350 professionals in 15 offices globally.

Vendor Financial Services (VFS) is a global leader in providing financial and service solutions to equipment manufacturers, dealers, distributors and end users. Vendor Financial Services serves more than 100 manufacturers, 6,000 dealer/distributors, and 700,000 end-users in over 23 countries.

Equipment Management

Americom is a leading global provider of satellite communications services to a diverse array of commercial and government customers, including the broadcast and cable TV industries, broadcast radio, and users of business information and communications network services. Americom operates 13 communications satellites and maintains a supporting network of earth stations, telemetry, tracking, and control facilities. It is expanding its international reach to all of Europe via GE-1E, and to South America through its investment in NahuelSAt. When GE-1A is launched in Asia next year, the Americom fleet will provide service to over 80% of the world's population. In addition, its GE Capital Spacenet Services subsidiary offers a full range of one-way and two-way Very Small Aperture Terminal (VSAT) products and global networking services.

Aviation Services (GECAS) is the world's largest aircraft leasing firm, with more than 900 planes and 160 customers in over 60 countries. With over 350 firm aircraft orders or options from Boeing and Airbus, GECAS provides a full range of aircraft financing products and services – including operating leases/loans, sale/lease backs, bare aircraft purchases/asset trading, finance leases, fleet planning/restructuring services, remarketing services and select capital markets services.

GE Capital Fleet Services is one of the leading corporate fleet management companies in North America, Japan, Europe and Australia, with approximately 940,000 cars and trucks under lease and service management. In addition to vehicle lease financing, Fleet Services also provides value-added management services, such as national account purchasing and fuel programs, title and licensing services, maintenance management, and accident management and prevention programs designed to reduce customers' total fleet management costs. The partial or complete outsourcing of the fleet management function to GE Capital Fleet Services allows companies to focus on what they do best. As a productivity partner, GE Capital Fleet Services' business helps others gain a competitive edge in their marketplace.

GE SeaCo is one of the world's premier marine container leasing companies. GE SeaCo provides its customers with a flexible and diverse fleet, ranging from standard dry containers to special use containers, such as refrigerated and non-hazardous tank containers. GE SeaCo, which combines the expertise of GE Capital and Sea Containers, is also at the forefront of technology solutions for its customers, including on-line booking and queries and global container tracking.

Information Technology Solutions (ITS) is one of the world's largest providers of PC-based products and services, a leading provider of IT consulting services, and a distributor of advanced

IT products. GE Capital IT Solutions partners with leading vendors to provide government and commercial customers with the best combination of PC, networking, software, and midrange products to meet their specific requirements. Through its consulting business, GE Capital IT Solutions provides advanced IT solutions, including application development in Microsoft, Oracle, and Sybase as well as sales force automation, business process re-engineering, enterprise office automation, financial and accounting services, and computer telephony. GE Capital IT Solutions is also building a distribution business to support over 10,000 Value-Added Resellers (VARs) worldwide with complex information technology solutions and products, including Sun, SGI, and CISCO.

Modular Space leases, rents, finances and sells mobile and modular buildings for a wide range of applications including construction, education, healthcare, business and industry, government, and financial services. It maintains a fleet of approximately 125,000 relocatable modular structures for rental, lease, and sale from over 100 sales and service locations in North America and Europe.

Penske Truck Leasing has 110,000 vehicles and offers a comprehensive range of full-service leasing, contract maintenance, truck, tractor and trailer rentals, integrated logistics, and warehouse distribution center management through approximately 600 locations in the United States, Canada and Europe.

Railcar Services is a leading railcar leasing company in North America, with the most diverse fleet in the industry. In addition to offering a variety of leasing alternatives, the company provides railcar management, repair, refurbishment, conversions, and other services to railroads and shippers in North America. In Europe, the company offers long- and short-term railcar hire, various rail transport services to the steel, automotive, paper, and other industries.

TIP (Transport International Pool) is a leading trailer specialist that rents, leases, buys, sells, and finances over-the-road commercial semi-trailers from over 270 branches worldwide. TIP's diverse trailer programs and quality value-added services help trucking companies, manufacturers, retailers, railroads and other companies improve trailer productivity, both operationally and financially. Its fleet includes over 235,000 dry freight vans, refrigerated vans, storage vans, flatbeds, intermodal trailers, containers, chassis and specialized trailers.

Consumer Services

Auto Financial Services (AFS) is a leading provider of innovative automotive financial service products in more than 22 countries around the globe. AFS provides new and used vehicle leasing, financing, and sub-prime financing to consumers through an extensive global network of more than 15,000 auto dealers. AFS also offers unique value-added commercial finance products to enhance a dealer's ability to meet the continuing growth challenges in the automotive industry. In addition, AFS has private label relationships with several leading auto manufacturers.

Consumer Financial Services (CFS) develops and markets consumer credit cards, including the GE Rewards MasterCard-GE Select Platinum VISA/MasterCard, Exxon Master-Card and International Wildlife Coalition MasterCard, and corporate credit cards including Purchasing cards, T&E cards and Fleet cards designed for medium and large-sized companies. CFS has worked with numerous companies to design tailor-made credit cards and other financing programs to meet specific customer needs and expand sales potential.

Consolidated Financial Insurance (CFI) is one of Europe's leading providers of specialist insurance and investment services, including payment protection insurance (PPI), operating in 14 countries worldwide. PPI is the group's core product, and CFI works in partnership with banks and other lending institutions to help ensure their customers' financial commitments are covered in the event of accident, sickness, death or unemployment. CFI has grown significantly in the last four years and is now the UK's thirteenth largest general insurance company (by premium income). The group continues to expand into other specialist areas of insurance including third party administration, travel, and pet healthcare. Its highly successful personal investments division was the UK's second largest provider of single premium insurance bonds in 1997.

GE Capital Australia and New Zealand operates 14 businesses across GE Capital's five main business categories: consumer services, equipment management, mid-market financing, specialized financing, and specialty insurance. These include Australia's leading private label credit card issuer, the largest home mortgage insurer, a major IT outsourcing provider, a nationwide pallet hire business, and the premier automotive fleet leasing company operating in Australia and New Zealand.

GE Capital Japan provides a wide array of innovative, quality financial services to individuals and businesses. Key products include: sales finance; private label credit cards and bankcards; personal loans and auto leasing; marine container leasing and related services; reinsurance services for property and casualty insurers, captives and life insurers; guaranty services for asset-backed securities; and life and other insurance products for individuals. GE Capital Japan also brings innovative real estate and commercial equipment financing as well as structured finance solutions to the Japanese marketplace.

GE Capital Mortgage Services is a national provider of residential financial services, supplying capital and mortgage products to lenders and borrowers, purchasing and servicing first- and second-mortgage loans, and serving as a major source of private mortgage-backed securities. Mortgage Services administers loan payments for more than one million homeowners through its $100 billion servicing portfolio, originates loans on a wholesale basis, and operates an active private mortgage conduit.

GE Financial Assurance (GEFA) has consolidated assets totaling $46 billion and provides financial security solutions that help consumers create, preserve, and protect their lifestyle and personal wealth. The businesses market fixed and variable annuities, life insurance, mutual funds, long-term care insurance, auto insurance and warranties, and supplementary accident and health products through financial institutions, independent life insurance agents, securities brokers, financial planners and career-agent sales forces.

Global Consumer Finance (GCF) is a leading provider of credit and insurance services to retailers and consumers in 25 countries around the world. It offers private label credit cards and proprietary credit services to premier retailers and manufacturers, as well as diversified financial programs including direct-to-consumer financial programs, personal loans, and MasterCard and Visa cards. GCF also offers consumer insurance services in 13 countries in Europe, Australia and Latin America through its Consolidated Financial Insurance business unit.

Retailer Financial Services (RFS) is a world leader in providing proprietary credit services to retailers and manufacturers throughout North America. With products such as private label credit cards, credit insurance and database marketing solutions, RFS serves more than 300 retailers and over 70 million cardholders. In addition, the company offers financial solutions including inventory financing, securitization, asset-backed lending, and strategic equity investing.

Specialty Insurance

Employers Reinsurance Corporation (ERC) has been a leading provider of Global Risk management and Financial Stability products for over a century. With 50 offices worldwide, the ERC companies rapidly respond to the needs of insurance companies, healthcare providers, self-insureds, and others. Whether the customer requires standard insurance products, alternative risk transfer techniques or financial market products, ERC provides cost-effective, tailored solutions.

Financial Guaranty Insurance Company (FGIC) and its affiliates offer state and local governments and government agencies products and services to strengthen their finances and operations, including municipal bond insurance (FGIC), property and casualty insurance (Coregis), guaranteed municipal investment contracts (FGIC Capital Market Services; unaffiliated companies Trinity Funding Company, LLC and Trinity Plus Funding Company, LLC) and revenue management services for the recovery of accounts outstanding (FGIC Government Services Inc., Great Lakes Collection Bureau, Inc. and SCA Credit, Inc.)

GE Capital Mortgage Insurance is a leading provider of private mortgage insurance, helping to expand the housing market by allowing borrowers to obtain low down-payment loans while minimizing risk for lenders and investors against mortgage default. In the US, Mortgage Insurance is aggressively pursuing nontraditional markets, such as portfolio lenders, with the aid of OmniScore, an in-house risk-management tool that will put home ownership within the reach of more creditworthy families. With operations in the US, Canada, the United Kingdom and Australia, Mortgage Insurance is transforming itself into the first truly global provider of integrated solutions for mortgage lenders.

To learn more about asset based financing solutions or about the other businesses of GE Capital, call us toll-free at **1-800-243-2222 ext. 98**, or visit our website at **http://www.gecommercialfinance.com**.

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