Difference Between Bill Discounting & Factoring

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Introduction

Both these words are types of short-term finance by which financial requirements can be meet immediately. Bill of discounting is the short term finance borrowing from the commercial banks while the factoring is related to the debts and how to manage it.

Bill Discounting

- Bill discounting is a method of trading or selling the bill of exchange to any financial institution like banks before it becomes matured with a less price than its par value.
- Discount on a bill of exchange is based on the remaining time for a maturity of it.
- A bill of discounting involves trade debts which are backed by account receivables.
- In simple language, Bill of discounting is an advance against the bill.

Process

Step - 1

The bank must satisfy itself about the credibility of the drawer before giving money.

Step – 2

A bank will deduct fees or discount from the granted money and then give the reaming money.

Step – 3

Once the bank purchases the bill of discounting it becomes an owner of the bills and if customer delays payment then he has to pay an interest rate to the bank at the directed rates.

Step – 4

If the customer does not pay bills on time and becomes a defaulter in that case bank has right over the goods or services provided by the borrower to the customer.

Factoring

- Factoring is a process in which the customer or borrower sells its debts to the financial institution or a factoring company at a discount.
- Factoring finance deals in account receivables it means invoices.
- A factoring company deducts the interest charges on financial services and commission charges for additional services from the factoring charges.
- A customer gives the instruction to transmit payment directly to the factoring company and settles the due balance.
- A factoring company provides the number of services to the customer like Credit Investigation, Debtors Ledger Maintenance, Collection of Debts, Credit Reports on Debtors and much more.

Process:

The factoring process mainly divided into two parts

Step - 1

The Initial account setup

It takes one to two weeks and includes various formalities like submitting an application, file of clients, report of invoices and a sample invoice.

Step – 2

Ongoing funding

This process comprises the detailed underwriting during the period in which the factoring company asks for additional papers like paper of incorporation, bank statements.

If it is approved the business will get a maximum credit line from which they can draw.

Difference Between Bill Discounting and Factoring

Basis	Bill discounting	Factoring
Meaning	Bill discounting means to trade bill before it becomes due for payment at par value.	Factoring means to sell its bool debt to the financial transaction to the factoring company at a discount.
Existence	Bill discounting comes under the Negotiable instrument act, 1881.	There is no such specific law for factoring.
Settlement of finance	In bill discounting, the bill is discounted and paid when the transaction takes place.	In factoring, the financer gives a maximum amount as an advance when a transaction takes place the remaining amount at the time of settlement.
Parties involved	In bill discounting there is a drawer, drawee, and a payee.	In factoring, there is a factoring company, debtor and a customer.
Fees	A financer charges fees in the form of discounting charges or interest.	Financer gets fees in the form of interest for the financial services and commission for extra services facilitate.