



## Post-Training Support

### How to Finance your Business

Start up loans a difficult to obtain from banks. Banks normally make loans only to businesses with operating histories. Personal savings should be considered the primary source of funds for starting a business. Begin to accumulate these funds now!

To obtain any loan from any financing organization, you must have an acceptable credit score. This number represents your credit worthiness. The FICO score is a numeric method, using three digits, to predict the likelihood of your paying your credit as agreed. FICO scores range from 365 (not good) to a high of 850 (great). The score evaluates your credit payment history, number of open accounts, overall credit balances and public records such as judgments and liens.

Generally, a FICO score of 680-720 will produce a positive response. Services like [www.myfico.com](http://www.myfico.com) will provide you with several report formats and notify you of credit inquiries that could affect your score. Before seeking financing or credit, it is a good idea to know where your FICO score stands.

#### Unsecured Loans

Some credit is granted on an unsecured basis, such as credit cards, but most small business loans are secured by the assets of your business, your personal assets, or both. Unsecured means that there is no collateral granted for the loan. Examples of unsecured are:

- Credit cards
- Unsecured lines of credit (like you get in the mail)
- Friends or relatives
- Secured Loans

#### Secured loans

Assets pledged to secure the payment in the event you are not able to pay. Examples of this are:

- Computer lease
- Home mortgage
- Car loan or lease
- Small Business Administration loan

#### Collateral

Common types of collateral are equity in your home, accounts receivable, inventory of the business and equipment. Lenders go through an evaluation of the collateral



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to determine how much they can lend against it. Some key variables as to what kind of loan terms you can get are:

- Number of years in business - This is your track record and is very important. Banks usually require three years while others are less stringent.
- Size of your company and the amount needed - Financing institutions vary in the way they service the public. For example, you would probably not get a car loan and a large corporate loan at the same place. Do your research. Ask around. Get to the right spot.

### **Loans (Debt) vs. Investment (Equity)**

You are most likely familiar with a straight loan (debt) where the lender gets an interest rate and fees.

Equity is where the money raised gives the investor an ownership interest. This is common in the sale of stock to a limited number of investors or participation by venture capitalists. The sale of stock is highly regulated by state and federal agencies and you will need the help of a corporate lawyer. Normally the initial sale of stock to the public (initial public offering or IPO) is deferred until an earnings history is established.

Sometimes such a discussion arises with friends and family who want to be your partner. Consider this carefully because they will then participate in the increased value of the business and have voting rights.

It is well beyond the scope of this discussion to cover all the aspects of debt and equity. Just be careful! Your lawyer and accountant would be appropriate sources for more information on this subject.

### **Where to Get the Money**

The chart below will show some differences between some of the types of lenders. Terms will vary considerably from lender to lender; the summaries in the chart are only meant to be representative and give you an idea of what to expect when seeking money from different sources. Important issues to consider:

- Cost
- Payback program
- Loan size



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Some of the pros and cons of the different lenders are briefly listed below. There will likely be one common characteristic among them all. As an entrepreneur, you will be legally obligated to have individual responsibility for the credit obligation of your business. Regardless of legal organization, lenders may want personal guarantee. This is very common.

Comparison Table					
Type	Cost	Payback Terms	Sizes	For	Against
Personal Savings	No cost	None		Easy, cheap	Risk of Loss
Friends & Family	good rate or none	Flexible,		best value	Can create friction
Mortgages Equity	7-9% 8-14%	Very long flexible	80-100%	Cheapest, longest terms	House at risk
Credit cards	16-23%	40-60 months	3,000-10,000	Easy qualifying, no collateral	Small amounts
Suppliers	Free	30 days +/-		Inexpensive unsecured	Short term
Landlord	Adds to rent cost	Over lease term		Preserves cash/assets	Hard to get
Venture capital	25-40%	5-7 years	\$500,000+	Large amounts	Very hard to get; share ownership
Commercial mortgage	7-9%	25 years	\$300,000+	75% of appraisal	all due in 10 years
Specialized lenders	12-18%	5-7 years	Varies	Accessible through dealers	High Debt service
Leasing companies	12-18%	5-7 years	Varies	100% financing through dealers	High Debt service
SBA loan guarantee	2% over bank rate	7-20 years- fully amortized	\$50,000-1,000,000+	Longest payback	Complex process
Finance companies	14-30%	1-3 years	\$100,000+	An alternative	Expensive; picky about collateral
Banks	6-9%	1-5 years	\$100,000+	Least expensive	Hardest to qualify

**Business Loans**



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This starts by knowing what your lender wants. A common way is to simply ask. A better way is to ask a friend or business advisor such as your CPA.

For a business loan, the most common things are:

- Business financial statements
- Business tax returns
- Business Plan with budget or projection
- Personal financial statements
- Personal tax returns

Step two is to be ready to answer questions about your business, and be ready to highlight your financial performance both in the past and in the future. You will be more impressive if you have carefully thought-out and become familiar with your plan. Bring your accountant if you need help.

Be prepared to tell them why you need the money. "I just need the money," does not inspire confidence or the fact that you have thought it through. Earlier in this session, you studied a number of different purposes. Give them some detail.

### Repayment Plans

Propose a repayment plan. Examples of different structures are:

- A line of credit, payable at your discretion but subject to renewal annually by the bank
- Term loan payable monthly over \_\_\_ years starting on \_\_\_ date
- Most places have some flexibility. Potential lenders appreciate that you are thinking about paying them back instead of just getting the money.
- Most lenders (including the SBA) will want to see your business plan.
- Keep your lenders informed on the status of your business: the good and the bad.
- If you are unable to make a loan payment on time, call your lender in advance, advise him/her of the problem and request the extension you need. Explain the sources of repayment.
- Virtually all lenders will do a personal savings and corporate credit check through a company called TRW or by other means. Be prepared to discuss any prior credit issues/problems. The best access to a lender is through a referral. Lending is a people business. Have your CPA, attorney, or friend introduce you to a lender.
- The first thing that will spook lenders or investors is the fear you are "puff" rather than "substance." Avoid giving the impression of being an over optimistic, "pie-in-the-sky" operator.



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- As a start-up, do not plan to spend money on expensive entertaining. Your lenders will be more interested in knowing how their money is being used to grow your business.
- Do not depend on a bank to loan you money to start a business. Most small businesses are funded by personal savings.
- Make a shrewd appraisal to minimize your risks and to limit losses to a predetermined limit.
- "Your suppliers and vendors can be sources of financing. For example, if you need an illuminated sign for your store front, the company you contract with to make the sign may provide financing so you can make monthly payments rather than pay cash. Examples of financing from your suppliers include:
  - Longer payment terms
  - Advertising and marketing assistance
  - Furnishing or financing of equipment, signs or inventory.
  - Advertising and promotional programs
  - Bartering, which is to trade by exchange one commodity for another, can provide a source of financing. For example, your advertisements in the local newspaper might be paid for by the bagels you make!

### **After You Obtain Funding**

Obtaining funding is the first step. You should strive to be a good customer so you can get cooperation if you need help later. Make sure you understand the requirements and perform to them as much as possible. In a business relationship, lenders will ask for regular financial statements, which you should produce on time. There may be covenants that require submission of periodic financial and operating statements. Contact your lender if there is a problem. Be sure to stay in touch even if nothing new is going on.

### **Notes**