

BUSINESS FUNDING

SOURCE CATALOG



Why You Need Financing to Grow Your Start-up Businesses:



Financing is needed to start a business and ramp it up to profitability. There are several sources to consider when looking for start-up financing. But first you need to consider how much money you need and when you will need it. The financial needs of a business will vary according to the type and size of the business. For example, processing businesses are usually capital intensive, requiring large amounts of capital. Retail businesses usually require less capital. Debt and equity are the two major sources of financing. Government grants to finance certain aspects of a business may be an option. Also, incentives may be available to locate in certain communities or encourage activities in particular industries. Banks are also a viable source, but they will be sure to ask for proof that your business has been operational for a number of years, and you'll need to show some kind of income and profit. They need to feel secure in lending to you.

Funding Your Dreams

Why are small businesses essential to the American economy?



The American economy has been built by entrepreneurs who were willing to take risks and explore new ventures. Ray Kroc was 52 years old when he purchased the rights to a hamburger stand owned by the McDonald brothers in San Bernardino, California. His venture would revolutionize the food industry. Robert Pittman was only 26 years old when he combined video and music and created MTV.

The funding of small businesses is essential to the American economy. Almost all of the nation's Fortune 500 companies started as small businesses. They began with little capital and obtained additional funds by using creativity. Today you can get funds through a variety of sources. Through private and public funding, you can pursue your dreams and own your own business.

Funding a Business

Why do many entrepreneurs need to find outside sources for funding?

One of the major concerns when starting a business is how it will be financed. People who take on new business ventures usually need far more money than they realize.

Jenny and Matt started their lemonade stand with nothing. They had no lemonade, supplies, or cash. They funded their business with cash and other assets that their families provided. They hoped to sell several cups of lemonade and take in some money. Do you think that they made a profit? Chances are that the money they took in did not cover the cost of the lemonade and other supplies.



Business Plan

The bank will also examine your business plan to make sure that your business is financially sound. It looks to see whether you have a clear vision of where you want your business to go and whether you have identified the necessary steps to achieve your goals. Then the bank can better measure your financial needs.

Banks often base loan decisions on the business plan. It is vital that your plan be clear, accurate, and well planned. Include the three basic parts of a business plan that focus on a strategic plan, a marketing plan, and a financial plan. Each plan is unique, and every business plan can include a variety of components, such as an executive summary, mission statement, company description, product and service plan, management team plan, industry overview, market analysis, competitive analysis, marketing plan, operational plan, organization plan, financial plan, growth plan, contingency plan, and supporting documents, as well as a cover page, title page, and table of contents. Spending extra time to make sure that your business plan has accurate information could mean the difference between getting the money you need or not.

Analyzing Financial Needs

Starting a New Business

What do you need to start a new business?

Jenny, age 8, and Matt, age 7, are going into business. They are going to set up a lemonade stand—called J & M Lemonade—in front of Matt’s house. A lot of people walk down that street, which is close to a school and a park. Jenny and Matt figure that their location will provide plenty of customers. It is summer, and people are thirsty. Cold lemonade will be in demand.

Before they begin selling lemonade, however, Jenny and Matt must decide what things they will need to get their business started. In addition to lemonade, Jenny says they will need a large pitcher, a stand or table, and some cups. Matt adds a large sign, a box for their money, and some ice cubes to the list. They agree that they will also need coins to make change for customers.

As with all business operations, Jenny and Matt will need cash, equipment, and supplies, as well as goods or services to sell. How do you think they will get these items? They will probably do what you did when you were their age: They will go home and see what they can find. Their families may help them find a pitcher, a table, and some cardboard to make a sign. They may give them some coins to use for change and buy the lemonade and cups.

Soon Jenny and Matt have all the items they need, and they set up their stand. J & M Lemonade is now an active player in the free enterprise system.

Business Entrepreneurs

What does it take to become an entrepreneur?

When you were younger, you may have had a small business similar to Jenny and Matt's lemonade stand. Like Jenny or Matt, you were an entrepreneur. An **entrepreneur** is an individual who takes the risk of starting a new business. Entrepreneurs are highly motivated people who transform ideas for products or services into real-world businesses. About 80 percent of the 23 million business operations in the United States are run by one owner. Entrepreneurs are the backbone of the American economy.

Most businesses fail because of
lack of planning & funding!

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Determining Needed Capital

Why is it so important to know how much money is needed to start up a business?

When you are starting a business, the first thing you must do is make a realistic estimate of how much capital you will need. As you know, capital is the money you need to establish a business, to operate it for the first few months, and to expand the business. Determining the capital needed to start up your business is one of the steps of developing a financial plan.

Start-Up Costs

The first goal in determining needed capital is to identify start-up costs. Start-up costs usually require a large amount of cash. If you attempt to estimate the costs without careful analysis, your estimate will probably be too low.

To analyze your costs, you should list everything you will require to begin to operate. Most businesses have some common start-up costs:

- Inventory needed to open the business
- Equipment, fixtures, and display cases
- Security deposit for rented space
- Advertising and promotions
- Insurance
- Professional fees (such as lawyers' fees)
- Remodeling costs (such as creating office space)
- Legal permits and licenses
- Supplies

Your next task is to assign an estimated cost to each item. Unless you list every anticipated cost, your total estimate will not be realistic.

Landscaping firms and convenience stores are different types of businesses, and each has different requirements for operating. Start-up costs vary among businesses and industries. Make sure that you research and explore the industry you are entering.

3 categories of operating costs



Fixed costs

Always occurs regardless of production

Ex: Rent



Variable costs

Increases with the amount of production

Ex: Utilities



Semi-variable costs

Has a flat cost, but increases with a production increase

Ex: Overtime pay

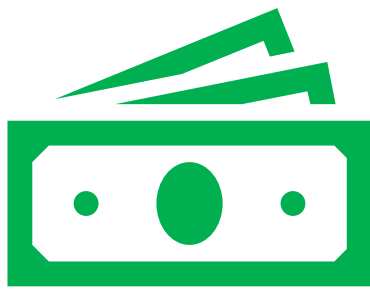
Operating Costs

Besides determining your start-up costs, you must also estimate your operating costs for the first 90 to 120 days. **Operating costs** are the ongoing expenses for operating a business.

Start-up costs and operating costs are separate cost categories. It is critical that you estimate both types of costs as accurately as possible. If you use all of your money for start-up costs, then you will not have any money available to pay your operating costs. When you start a new business, the amount you earn usually will not be enough to cover your expenses. If you cannot pay your suppliers, rent, or utility bills, your business will be in serious trouble.

When you prepare your budget for the first 90 to 120 days of business, you will include your expected income as well as your estimated monthly costs. Businesses have a number of common operating costs:

- Payroll
- Rent
- Insurance premiums
- Utility bills
- Office expenses
- Advertising
- Delivery charges
- Bank charges and other fees



Reserve Fund

Before starting a business, you will also have to estimate the amount of money you may need at a later date for growth. A **reserve fund** is money that can be made available for the future expansion of a business. You may need additional money to purchase merchandise or equipment, or perhaps to lease a truck. This money will allow for growth and help you avoid having to borrow additional capital.

Jenny and Matt's lemonade stand stayed in business for only two hours. They did not plan to operate an ongoing business. Of course, you hope that your business will have a much longer life. Therefore, careful financial planning for the future is critical. Consider other expenses when looking ahead and estimating a reserve fund:

- Additional equipment for increased business
- Advertising and other promotional costs
- Capital for any unexpected costs or decreased sales
- Maintaining a positive cash flow
- Expansion of facilities
- Getting and keeping the right amount of inventory

When you have estimated the amounts of your start-up and operating costs and your reserve fund, you will have a good idea of your business's financial needs. You will see what your cash flow will look like during the first months of operation. Then you can estimate the total amount of capital you will need to establish your business and begin to operate.

Sources of Funding

Small Business Administration

What kinds of services does the Small Business Administration provide?

No matter how good your business may look on paper, banks might not provide necessary financing. This is especially true for new or start-up businesses. As a new or start-up business owner, you may not have a sound credit history or enough collateral, managerial experience, or profit from operations. Therefore, you will need some help to get your loan. To whom do you turn? Your best alternative may be the federal government.

The federal government recognizes the importance of small businesses in the American economy and, therefore, provides assistance to them. The **Small Business Administration (SBA)** is an independent agency of the federal government that offers assistance to people who are starting small businesses and to those who want to expand existing businesses. Its services include management training, organizational guidance, and assistance in getting funding.

Almost 99 percent of American business operations are considered “small businesses” under the SBA guidelines. Thousands of businesses take advantage of services offered by the SBA every year. If the SBA did not exist, many small businesses would never get the money they need.

The SBA offers many loan programs to small businesses that have a hard time getting the funding they need through other methods. If you cannot convince the bank that you are a good loan candidate and that your business will be successful, you might try one of the SBA loan programs.

Investigate: An Application for Business Loan

An application for a loan from the Small Business Administration (SBA) contains:

- Name and contact information
- Amount requested
- Intended use of loan
- Other outstanding federal loans or debt

Your Motive: By applying for a loan through the SBA, you will have a better chance of receiving the funding you need to start your business.

U.S. Small Business Administration APPLICATION FOR BUSINESS LOAN					
Individual Jason True		Full Address 1647 West Alvarez, Phoenix, AZ 85001			
Name of Applicant Business True Business Forms				Tax I.D. No. or SSN	
Full Street Address of Business 5743 Sun Palm Lane				Tel. No. (Inc. A/C) 480-672-1853	
City Phoenix	County Maricopa	State AZ	Zip 85001	Number of Employees (including subsidiaries and affiliates)	
Type of Business Business to Business		Date Business Established		At Time of Application 14	
Bank of Business Account and Address First Merit 5812 Tuscan Lane # 3006482-1 Phoenix, AZ 85001				If Loan is Approved 22	
Use of Proceeds (Enter Gross Dollar Amount Round to the Nearest Hundreds)		Loan Requested		Use of Proceeds (Enter Gross Dollar Amount Round to the Nearest Hundreds)	
Land Acquisition		\$ 150,000		Pay off SBA Loans	
New Construction/Expansion/Repair		\$ 250,000		Pay off Bank Loans (Non SBA Associated)	
Acquisition and/or Repair Machinery and Equipment				Other Debt Payment (Non SBA Associated)	
Inventory Purchase				All Other	
Working Capital (including Accounts Payable)				Total Loan Requested	
Acquisition of Existing Business				\$ 400,000	
				Term of Loan (Requested Max.)	
				10 Yrs.	
PREVIOUS SBA OR OTHER FEDERAL GOVERNMENT DEBT: If you or any principals or affiliates have 1) ever requested Government financing or 2) are delinquent on the repayment of any Federal Debt complete the following:					
Name of Agency	Original Amount of Loan	Date of Request	Approved or Declined	Balance	Current or Past Due
SBA	\$100,000	6/28/20--	Approved	\$12,500	Current
	\$			\$	

Key Points: In order to be granted a loan by the SBA, you need to provide a personal financial history, inform them of the amount of the loan you are requesting, and describe how you intend to use the funds. The example represents just a small portion of the full Application for Business Loan.

Find the Solutions

1. How many employees will this company have if the loan is approved?
2. How will this company utilize the funds?
3. What is the total amount of the loan?
4. How much does this company owe the SBA for a previous loan?
5. What is the requested term of the loan?



U.S. Small Business Administration

SBA-Guaranteed Loans



Lending Partner



Loan



Small Business



U.S. Small Business Administration



8(a) Business Development

The federal government tries to award at least 5% of all federal contracting dollars to small disadvantaged businesses each year.



HUBZone

The federal government tries to award at least 3% of all federal prime contracting dollars to HUBZone-certified small businesses each year.



Women-Owned Small Business

The federal government tries to award at least 5% of all federal contracting dollars to women-owned small businesses each year.



Service-Disabled Veteran-Owned

The federal government tries to award at least 3% of annual federal contracting dollars to service-disabled veteran-owned small businesses.

SBA Guaranteed Loans

What is the benefit of receiving an SBA guaranteed loan?

The most common type of SBA loan is obtained through the Guaranteed Loan Program. To get an SBA guaranteed loan for your small business, you apply to a bank or other financial institution for a commercial loan. If the bank denies your request, you can then complete an application for an SBA loan. Your bank submits your application to the SBA under the Guaranteed Loan Program.

BENEFITS OF USING SBA LOAN PROGRAMS



Availability of capital



Low-interest rates



Helpful term length



Lower down payment



SBA resources partners' access

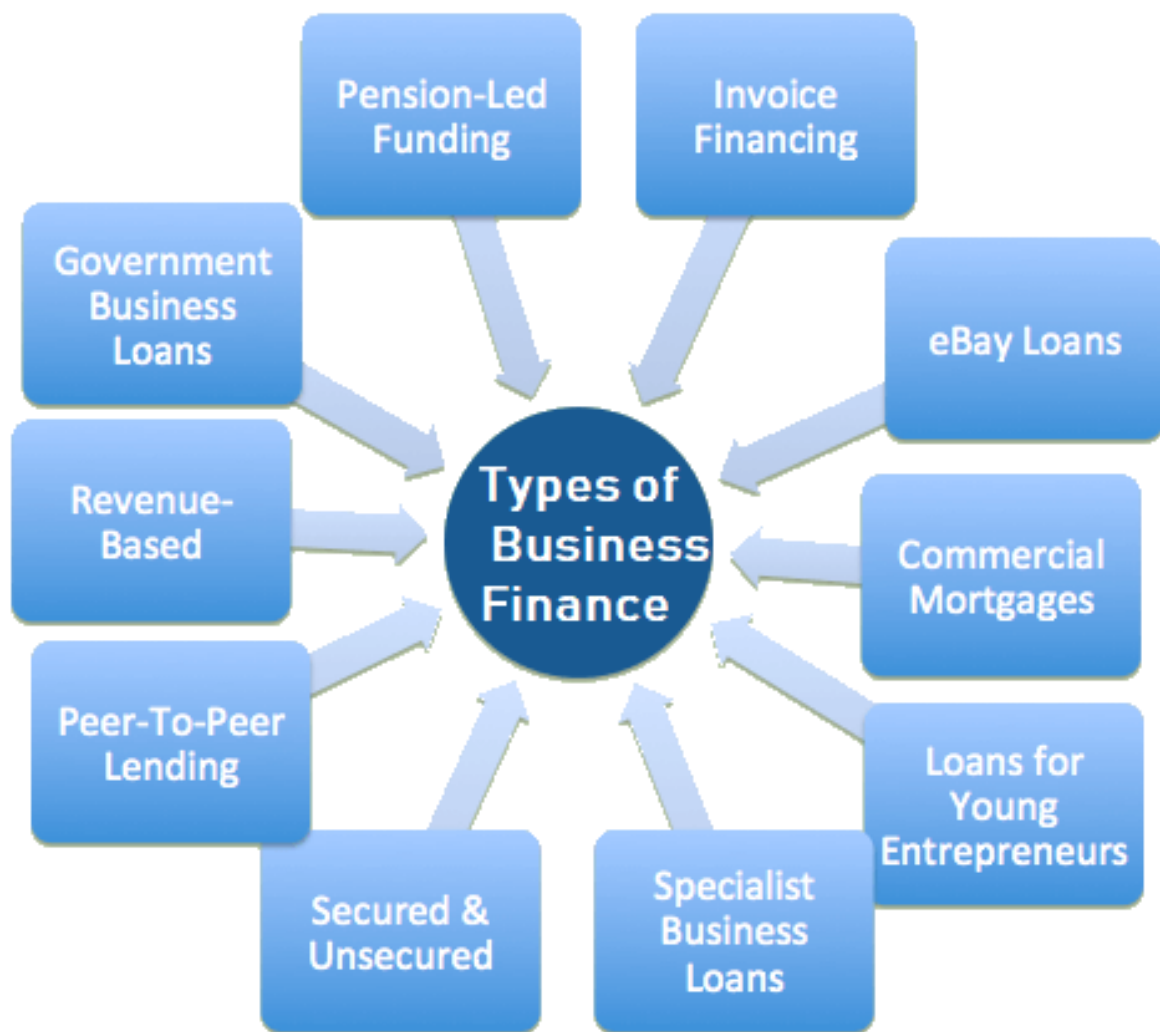


U.S. Small Business
Administration

Tips for Success

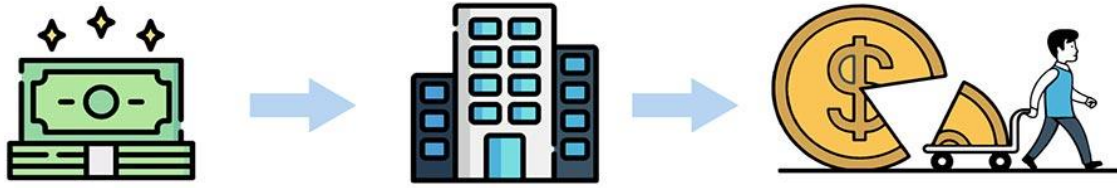
Doing Business with the Federal Government—**STRATEGIZE!**

- Determine who buys what you sell
- Is the market large enough for you to be profitable?
- Prioritize your buying targets
- Determine which certifications you need to be competitive with your target buyers
- Determine if you need or could use a partner
- Strategize over potential partners
- Consider Subcontracting
- Identify potential primes to target for collaboration (Joint Venture or Mentor-Protégé)
- **Create a plan** including these elements **with timelines for completion**

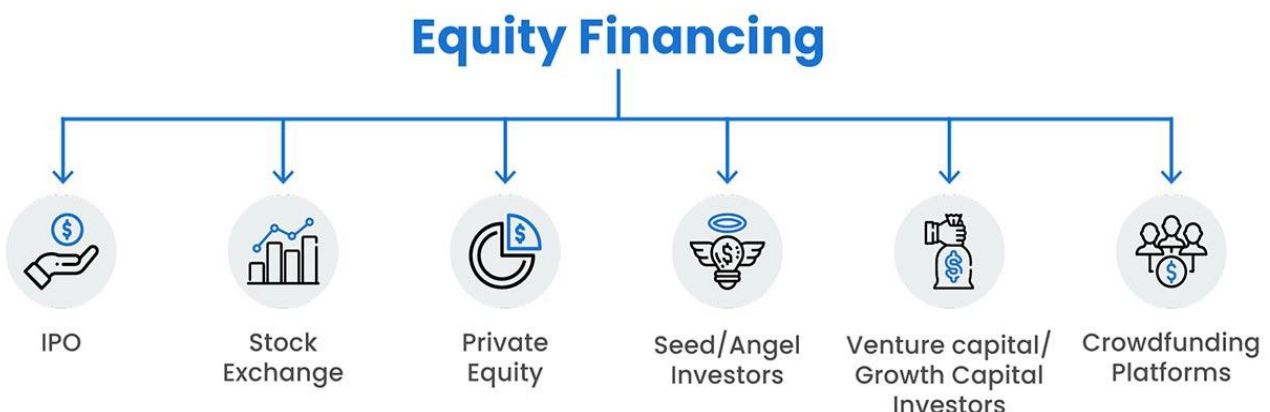


The financial needs of a business will vary according to the type and size of the business. For example, processing businesses are usually capital intensive, requiring large amounts of capital. Retail businesses usually require less capital. **Debt and equity** are the two major sources of financing. In addition to funding provided by the SBA, there are **Government grants** available to finance certain aspects of a business that may be an option for your business. Also, incentives may be available to develop your business in certain communities or encourage activities in particular industries. There is even funding available for specific people or nationalities, and social economic standing.

Equity Financing



Equity financing means exchanging a portion of the ownership of the business for a financial investment in the business. The ownership stake resulting from an equity investment allows the investor to share in the company's profits. Equity involves a permanent investment in a company and is not repaid by the company at a later date. The investment should be properly defined in a formally created business entity. An equity stake in a company can be in the form of membership units, as in the case of a limited liability company or in the form of common or preferred stock as in a corporation. Companies may establish different classes of stock to control voting rights among shareholders. Similarly, companies may use different types of preferred stock. For example, common stockholders can vote while preferred stockholders generally cannot. But common stockholders are last in line for the company's assets in case of default or bankruptcy. Preferred stockholders receive a predetermined dividend before common stockholders receive a dividend.



Personal and Private Financing

What is the difference between personal and private financing?

After you have determined the amount of money you require, you will need to figure out how you will get it. Getting affordable and sufficient financing is often a major problem when starting or expanding a business. However, there are many sources of funding available for businesses. Initially, you will probably explore the possibility of personal financing.

Personal Financing

Many people begin small businesses with funds from their own personal assets. In fact, personal assets make up a large part of the start-up funding for most new business ventures in the United States.

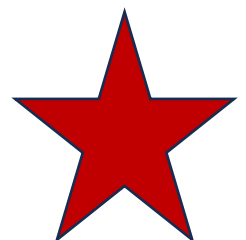
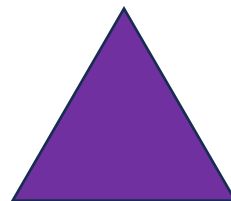
The primary reason for using this method is that new small businesses often have difficulty getting affordable funding. Banks and other financial institutions are not interested in risky or unproven business ventures. You cannot just walk into a bank and tell them that you have a great idea for a new business and expect the loan officer to hand you money.

Banks are more interested in funding existing businesses that have reported profit over a period of time. These businesses are safer investments and provide banks and other financial institutions with the assurance of a good return on their money.

When starting a small business, you may have to rely on your own assets to finance the start-up and operating costs. You might use your personal savings or investments such as stocks or bonds.

The Process of Raising Capital from Private Investors

- 01 Define Your Funding Needs
- 02 Develop a Funding Plan
- 03 Find Potential Investors
- 04 Negotiate Terms
- 05 Close the Deal



Private Investors

A **private investor** is a person outside an entrepreneur's circle of friends and relatives who provides funding because he or she is interested in helping a new business to succeed. Typically called "angels," private investors will usually leave the management of the business to the owner. However, they are also interested in getting a good return on their money. This means that you may have to give them a share of ownership.

If you cannot locate private investors in your area, you can turn to the SBA. The SBA has set up the Angel Capital Electronic Network (ACE-Net), which is a Web site that lists small businesses that are looking for investors. The SBA screens both entrepreneurs and investors to assure reliability. Approved investors can access information on thousands of businesses. An investor chooses a business, and then the business owner and the investor can negotiate a deal.

Private Financing

If you cannot get enough capital through personal financing, you must look to other sources. The next option might be private financing. **Private financing** is borrowing money from family or friends. This type of funding is attractive because it involves little paperwork and often requires no collateral and low, or no, interest payments. The disadvantage is that it can lead to personal conflicts if the business is unsuccessful, and you are unable to repay a loan.

Bank Funding

What is the difference between a secured and an unsecured loan?

If personal and private financing are insufficient, you may have to apply for a business loan to get additional money. One of your first sources for such financing is your local bank.

Commercial debt financing is borrowing money from a bank or other financial institution to fund a business. Another option is a **commercial loan**, which is a loan that finances a new or ongoing business. Larger banks give out commercial loans, but they are often interested in larger, more established business operations with revenues of millions of dollars. Therefore, when small businesses need money, smaller, local banks are their logical source.



Commercial Finance Companies

A **commercial finance company** is a firm that lends money only to businesses. Commercial finance companies insist that all loans be secured with collateral, such as equipment or inventory. These companies are helpful to existing businesses that need short-term financing.

The government does not regulate commercial finance companies as closely as it does banks, so these companies accept more risk in granting loans. However, if a finance company grants you a riskier loan, it will charge you a higher interest rate. It is easier to get this kind of loan, but you will pay more for it.

Venture Capital Firms

A **venture capital firm** is a company that provides private funding for small businesses that need a substantial amount of immediate cash. Because these small businesses are high-risk in terms of ability to repay loans, they cannot always get adequate funding from lenders such as banks and commercial finance companies. Venture capital firms take the risk, but in turn, they often expect a large return of 25 to 40 percent on their investment.

Venture capital firms usually seek to make investments of at least \$500,000. Keep in mind that the venture capital firm is not merely lending money; it is also investing in your business. Therefore, venture capital firms expect to have a voice in major business decisions and will examine a business's financial position carefully throughout the year.

Most venture capital firms are private, but the SBA created a public venture capital program—the Small Business Investment Company Program. **Small Business Investment Companies (SBICs)** are private investment firms that work with the SBA to provide longer-term funding for small businesses. The advantage in dealing with the SBIC program is that the SBA regulates lenders, and financing terms must meet SBA guidelines. If small businesses need venture capital, they usually go to SBIC firms first.

Secured and Unsecured Loans

A **secured loan** is a loan that is backed by collateral. Most short-term and long-term loans must be backed by collateral. Banks will hold the title to the equipment, facility, or merchandise used as collateral until the loan is repaid. Because banks must be conservative in their loan policies, most business loans are secured. Only a well-established, profitable business that has a good relationship with a bank can obtain unsecured loans. An **unsecured loan** is a loan that does not require collateral from the borrower. If an unsecured loan is approved, it is usually short-term. Because of the increased risk to the creditor, the interest rate on an unsecured loan is usually higher than on a secured loan.

Commercial Loan Applications

What are the five C's of credit?

New and expanding small businesses often have difficulty getting necessary funding. Banks use certain standards to judge a company's financial position and determine how much risk to accept. Banks are conservative and selective as to which businesses they approve for financing.

You have already learned about the criteria banks and credit card companies use to determine your creditworthiness (see Chapter 6). When you fill out an application for credit, you must answer questions regarding your credit history, your annual income, and your valuable assets. These institutions want a complete financial picture of you.

When evaluating commercial loan applications, banks will examine these same factors as well as other information. They want a financial picture of both you and your business.



Five C's of Credit

1. Character

2. Capacity

3. Capital

4. Collateral

5. Credit History

Assessing Credit Risk

Banks look at your five C's of credit to determine whether they should grant you a loan.

► **THE FIVE C'S** A loan officer will look carefully at the information you provide before deciding to grant you a commercial loan. *What criteria does a bank use to evaluate a loan request?*

How would you rate each one of your own five C's?

The Five C's of Credit

If you apply for a commercial loan, the bank will first examine the five C's of credit: character, capacity, capital, collateral, and credit history.

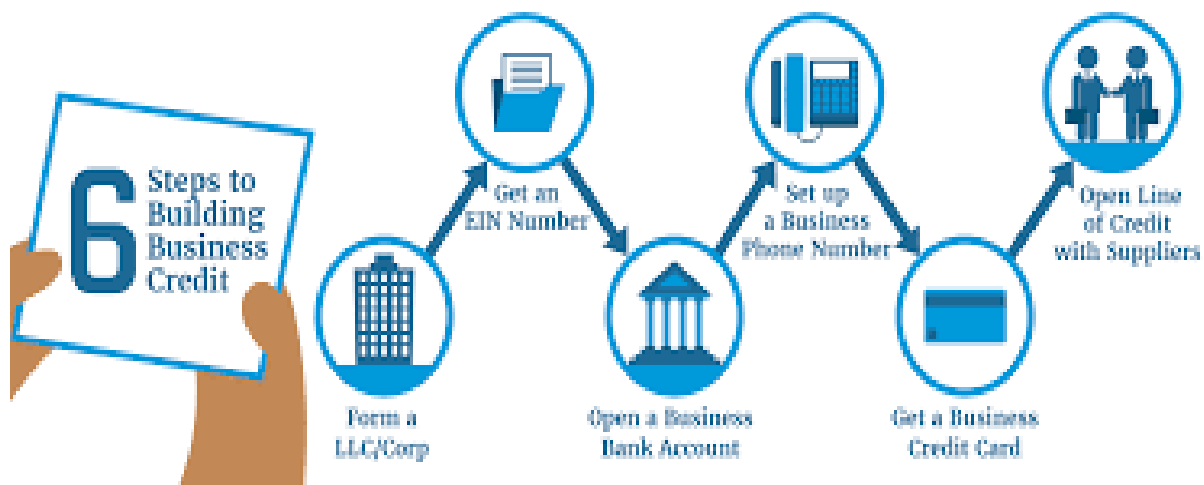
Character Banks want to make sure that you are capable of paying off the loan on time. They will consider your business experience and your dealings with other local businesses. Your prior history with the bank, your reputation in the local business community, and comments from your creditors will also be important. In addition, proof of your skills as a manager will be essential.

Capacity The bank will determine whether your business has or will have enough cash to repay the loan on time. It will also examine your sales history, statements of cash flow, and profits reported by your business.

Capital The bank will look to see whether you have invested a considerable amount of your personal assets in the business. Some financial institutions require that you use your personal assets for at least 30 percent of the capital needed to start your business.

Collateral The bank will make sure that you have enough business assets to secure the loan. Does your business own office equipment, machinery, delivery equipment, or real estate? Good collateral is also an important element for approval.

Credit History The bank will review both your personal credit history and your business credit history. It will also consider your payment history on any consumer and commercial loans you may have.



1

Structure your business as an LLC, C Corp or S Corp

2

Apply for an Employer Identification Number (EIN)

3

Open a Business Bank Account

4

Set Up a Business Phone Number

5

Get a Business Credit Card

6

Open a Line of Credit with Suppliers

Other Sources of Funding

Why might a new business need to obtain funding from other sources?

Some business owners use personal resources or funds from family members or friends to expand their businesses. Many others use short-term commercial loans, which are often guaranteed by the SBA. However, you can also get funding through a business credit card, private investors, commercial finance companies, venture capital firms, and state and local governments.

Business Credit Card

In recent years financial institutions have developed alternative funding options to try to meet the needs of a wide variety of businesses. One of these options is to offer a line of credit through a business credit card. A **business credit card** is a credit card that is issued to a business rather than to an individual. The use of business credit cards has become a major source of short-term financing for small businesses. Commercial loans from financial institutions are another common source of funding.

Business credit cards require the business to have a good credit history. They are suitable for businesses that want to expand or cover unexpected costs, but they are generally not issued for start-up financing. A credit limit on a business credit card is usually under \$15,000. The disadvantage of this quick source of funding is high interest rates, similar to those on personal credit cards. Business credit cards are good for emergencies, but balances should be paid as quickly as possible.

Visa, MasterCard, and American Express all offer small business credit cards. These cards provide discounts on travel, car rentals, and insurance. Credit card issuers also provide advice and assistance through small business publications.

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Personal Financing

Many people begin small businesses with funds from their own personal assets. In fact, personal assets make up a large part of the start-up funding for most new business ventures in the United States.

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Banks are more interested in funding existing businesses that have reported profit over a period of time. These businesses are safer investments and provide banks and other financial institutions with the assurance of a good return on their money.

When starting a small business, you may have to rely on your own assets to finance the start-up and operating costs. You might use your personal savings or investments such as stocks or bonds.

You might also use loans from family members and friends to help finance the business. However, with these sources of capital, you may not have enough cash to get the business going.

Consumer Loans In order to get the funds you need, consider applying for a consumer, or personal, loan. Most financial institutions require that consumer loans be secured with collateral. Collateral is a form of security (usually an asset such as a car or home) that helps guarantee that a loan will be repaid.

When you pledge collateral for a loan, the risk to the bank is reduced. As a result, you have a much better chance of getting funding and can receive better interest rates. If you cannot pay back the loan, the financial institution can take the property that you have pledged as collateral.

Home Equity Loans A home equity loan is a loan based on the difference between the current market value of a home and the amount still owed on the mortgage. A home equity loan may also be called a second mortgage. Home equity loans are fairly safe for financial institutions because they are secured by property. As a result these loans are usually easier to get than consumer loans, and some entrepreneurs who own homes use this source.

To determine the maximum amount of this type of loan, the financial institution will find out the current market value of a home and its equity. Equity is the value of the home less the current balance on the home's mortgage loan.

Suppose a house has a present market value of \$175,000, and the mortgage has a balance of \$65,000. The equity in the house is \$110,000 ($\$175,000 - \$65,000 = \$110,000$).

Banks will usually allow an owner to borrow up to 80 percent of the current market value of the home. In this example, the maximum amount the bank would loan on a home worth \$175,000 would be \$140,000 ($\$175,000 \times .80$ or $80\% = \$140,000$). However, there is an existing mortgage with a current balance of \$65,000. Therefore, to figure out the amount that the bank would loan, subtract the mortgage balance from \$140,000. In this example, the loan cannot exceed \$75,000 ($\$140,000 - \$65,000 = \$75,000$).



GO FIGURE

FINANCIAL MATH

A HOME EQUITY LOAN

Synopsis: Home equity loans are based on the difference between the current market value of a home and the amount still owed on the mortgage.

Example: Drew wants to apply for a home equity loan at Wilton Bank to start his new Internet company. He presently owns a home that has a market value of \$160,000. He has an existing mortgage balance of \$90,000. What is the maximum amount the bank will lend to Drew for a home equity loan?

Formula:

$$\text{Adjusted Market Value of Home} - \text{Existing Mortgage Balance} = \text{Home Equity Loan}$$

Solution:

A. Find the adjusted market value of the home.

$$\begin{array}{rcl} \text{Market Value} & \times .80 \text{ or } 80\% & = \text{Adjusted Market Value of Home} \\ \$160,000 & \times .80 \text{ or } 80\% & = \$128,000 \end{array}$$

The adjusted market value of the home is \$128,000.

B. Find the maximum amount of the home equity loan.

$$\begin{array}{rcl} \text{Adjusted Market Value of Home} & - & \text{Existing Mortgage Balance} = \text{Home Equity Loan} \\ \$128,000 & - & \$90,000 = \$38,000 \end{array}$$

Wilton Bank will lend Drew up to \$38,000 for a home equity loan.

YOU FIGURE

If the adjusted market value of your home is \$220,000 and the existing mortgage balance is \$142,000, how much would you be allowed to borrow for a home equity loan?

Private Financing

If you cannot get enough capital through personal financing, you must look to other sources. The next option might be private financing. **Private financing** is borrowing money from family or friends. This type of funding is attractive because it involves little paperwork and often requires no collateral and low, or no, interest payments. The disadvantage is that it can lead to personal conflicts if the business is unsuccessful, and you are unable to repay a loan.

Bank Funding

What is the difference between a secured and an unsecured loan?

If personal and private financing are insufficient, you may have to apply for a business loan to get additional money. One of your first sources for such financing is your local bank.

Commercial debt financing is borrowing money from a bank or other financial institution to fund a business. Another option is a **commercial loan**, which is a loan that finances a new or ongoing business. Larger banks give out commercial loans, but they are often interested in larger, more established business operations with revenues of millions of dollars. Therefore, when small businesses need money, smaller, local banks are their logical source.

A small bank can better relate to small business needs, and it can offer advice and assist you with other services.

Getting funding from local banks has both advantages and disadvantages. Advantages might include:

- They are highly experienced in dealing with small businesses.
- They offer a wide variety of loan plans.
- They offer advice and other business services.
- They are community-oriented and are interested in seeing local businesses succeed.



Disadvantages might include:

- They are closely regulated by the government. As a result, there is extensive paperwork, investigation, and documentation involved in the loan process.
- They are conservative by nature and may reject your loan if your business appears too risky.

If you and your local bank are interested in establishing a working relationship, you should know what loan options are available. All banks offer a wide variety of loans, and a good banker will recommend the loan that is best for you and your business.

Short-Term Commercial Loans

A short-term commercial loan is a business loan that is usually made for a term of one year or less. Most are written for 30-, 60-, or 90-day periods. These loans are typical for small businesses. They are designed to help the business meet short-term financial obligations and help with cash flow during a specific time or season. You could use the money for purchasing merchandise before a peak sales period, acquiring equipment, or paying unexpected bills.

For example, during the summer months, Durango's Ski Shop begins to prepare its inventory for the upcoming winter season. The owner, Sabrina, decides that she needs a large quantity of new skis. Because the ski shop's sales are typically low in the summer, she has to apply for temporary financing. With a short-term commercial loan, Sabrina can purchase the inventory she needs now and repay the loan with the profits from winter ski sales.

Long-Term Commercial Loans

A long-term commercial loan is a business loan that is made for a term of one to five years. These loans are normally used by larger, established businesses that require great amounts of funding. Because these are large loans, the businesses will need more time to pay them back. They may use the funds for expensive equipment, the relocation of facilities, the expansion of storage areas, or other major expenses.

New or smaller businesses might have trouble getting these loans. Banks consider such businesses to be less stable. Therefore, banks do not want to take the risk that the loan will not be repaid.

Lines of Credit

A **line of credit** is an arrangement in which bank customers can borrow a certain amount of money from the bank immediately. This makes funds available for unexpected costs or routine expenses. A store owner can borrow all or part of that money at any time and for any purpose. For example, if the plumbing breaks and costs \$8,000 to repair, money is available.

The main advantage of this type of funding is that you do not pay any interest unless you access the funds. But once you borrow an amount from the line of credit, the bank will charge you interest.

The bank will review your available credit every so often. Based on your history of accessing the account and on your repayment pattern, the bank may increase or decrease the amount of credit. This type of funding is intended for short-term costs that your business may not be able to handle. For this reason, the bank also expects you to repay the money in a short period of time.



It's also a good idea to establish a line of credit with companies such as **Uline, Quill and Granger**, because they will extend to a new start up a line of vendor credit called **Net 30**. This credit is a great way to establish business credit. It works like this: you open a business account with them and purchase a minimum amount of merchandise on credit. Then when the first invoice comes in, be sure to pay it on time. This will establish credit credibility, but best of all, they report to Dun & Bradstreet, which is a highly rated business credit reporting company.

Create a Uline Account

New Customers: Go online to ULINE.COM and sign up as a NEW CUSTOMER. You will be provided a CUSTOMER #. After ordering, use your customer number when prompted. Select "Invoice Me" during the checkout process. Qualified business customers will receive a net billing account, which allows for payment within 30 days of receiving the invoice.

Existing Customers: Sign in/Register online using your customer number to request a net billing account. If qualified, you can select "Invoice Me" during the checkout process.

If further information is needed, our Credit Department will reach out to you promptly. If you have any questions, call 1-800-295-5510 to set up an account and request terms. They will handle your request immediately.

Request Net 30 Terms with Quill

1. Go to Quill.com and place an online order of at least \$100 (before tax) and follow these steps:
2. At the payment step of checkout, select the 'Invoice My Account' option.
3. The first time you choose this option, we'll ask that you complete a form with your business's details (please fill out every field for quickest results).
4. After you submit your order, you will receive an email within a few minutes alerting you whether you've been approved or not. In some cases, your status will be “pending” and you'll be notified on your approval within 24 hours.
5. We'll then run a credit check of your business. This typically takes less than 24 hours.
6. Once approved, your order will be confirmed and shipped.
7. In cases where additional information may be required or we are unable to extend a credit limit, a member of our Credit Department will contact you and the order must be pre-paid by credit card.

If we are unable to extend terms, businesses may pre-pay for 90 days of consecutive ordering to establish history. After that time, our team will review your account again for credit terms eligibility based on the expenditure of the preliminary 90 days.

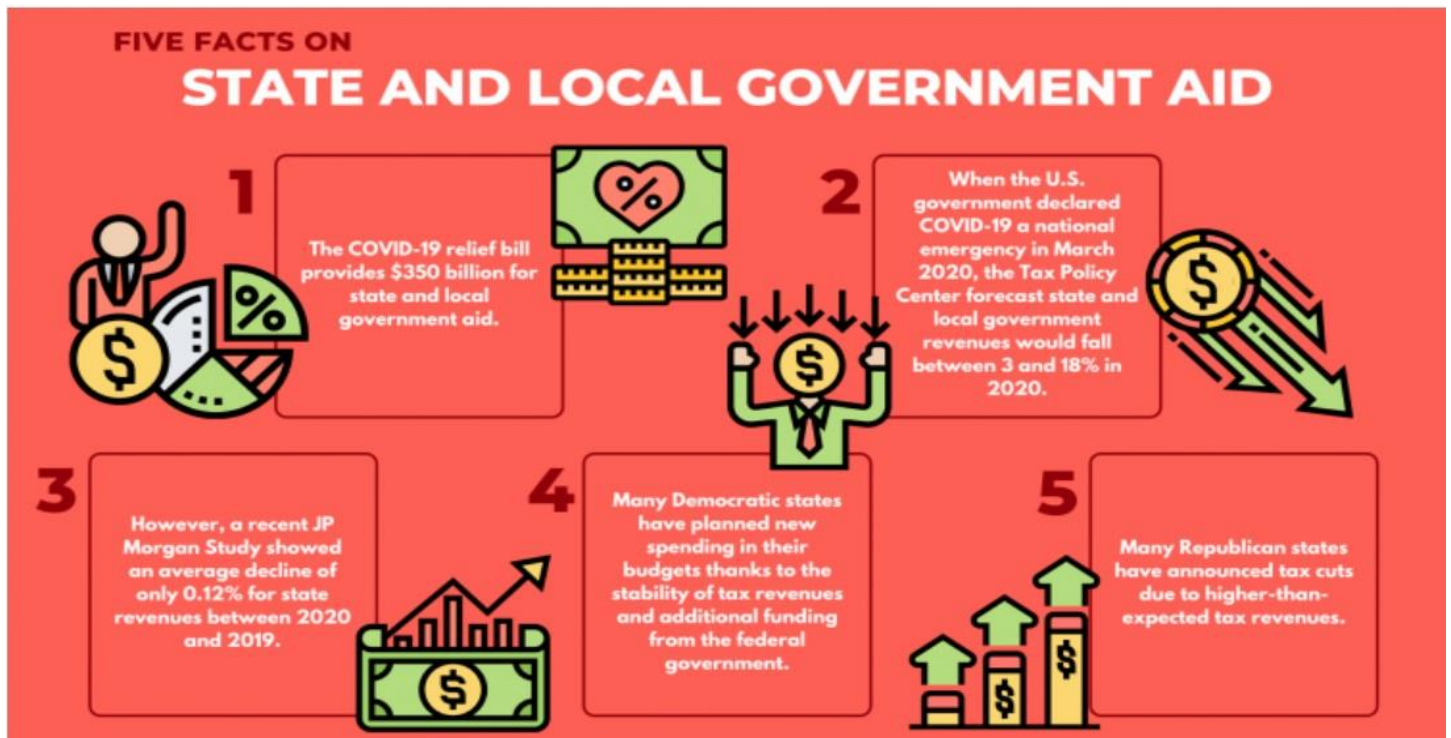
Registering with Grainger

Why do customers choose Grainger?

Their slogan says “We’re here to serve you, the ones who get it done”. More than 3.5 million customers rely on their:

- **Wide range of products:** Grainger has what you need – over 1.5 million products.
- **Fast shipping:** Get your order delivered when you need it – next-day delivery on most orders*
- **Helpful support:** Live-person support by phone, online chat or in person at over 250 branch locations
- **Strategic services:** Get help with safety and facility services, inventory management and much more.
- **Save favorite items to personalized lists.**
- **Create and view your customized account information.**
- **Track order status and order history from your dashboard.**

To register for a business account, visit [GRAINGER.COM](https://www.grainger.com), click on the REGISTER Tab, then select REGISTER AND CREATE A NEW BUSINESS ACCOUNT from the registration type drop down box and complete the requested information.



State and Local Funding

Why do state and local governments provide funding opportunities for small businesses?

Many states provide opportunities for small businesses to get funding through a variety of programs. These funding programs are available in cities where local and state governments are encouraging individuals to open businesses in economically depressed neighborhoods. Local chambers of commerce or regional offices of the SBA can assist you.

Using Grants to Fund Your Business

Startup business grants can help small businesses grow without debt. Be aware that competition for small-business grants is fierce, and many awards require time in business, often at least six months.

Some grants are open to newer businesses or true startups. And even if you don't qualify now, it can pay to know where to look for future funding. Here are the best grants for small-business startups, plus alternative sources of startup funding to consider.

Government Startup Business Grants and Resources

The Four Main Types of Federal Grant Funding

Competitive Funding

Formula Funding

Continuation Funding

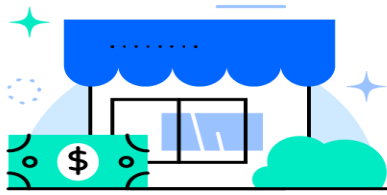
Pass-Through Funding

Some government programs offer direct funding to startups looking for business grants, but those that don't may point you in the right direction or help with applications:

[Grants.gov](https://www.grants.gov/)- Government agencies routinely post new grant opportunities on this centralized database. If you see an opportunity relevant to your business idea, you can check if startups are eligible. Many of these grants deal with scientific or pharmaceutical research, though, so they may not be relevant to Main Street businesses.

Local governments- Lots of federal grants award funding to other governments, like states or cities, or to nonprofit economic development organizations. Those entities then offer grants to local businesses. Plugging into your local startup ecosystem can help you stay on top of these opportunities.

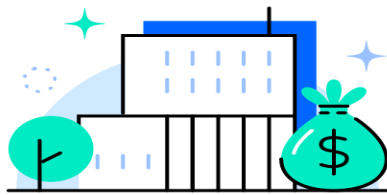
4 Types of Grants Available



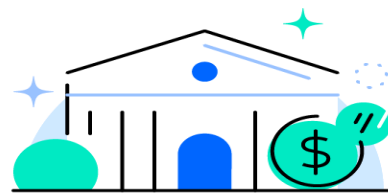
Local



State



Corporate



Federal

Small Business Innovation Research, or SBIR, and Small Business Technology Transfer, or STTR, programs- These federal grant programs are designed for businesses with innovative technology or scientific research ideas. Federal agencies list the types of research they're hoping to fund, and if you think your idea qualifies, you can submit a proposal. Unsolicited proposals aren't allowed.

Small Business Development Centers- These resource centers funded by the Small Business Administration offer business coaching, education, technical support and networking opportunities. They may also be able to help you apply for small-business grants, develop a [business plan](#) and level up your business in other ways.

Local startup business grants

Some local business incubators or accelerators offer business grants or pitch competitions with cash prizes. To find these institutions near you, do an online search for “Your City business incubator.”

Even if you don’t see a grant program, sign up for their email newsletter or follow them on social media. Like SBDCs and MBDA, business incubators often provide [business coaching](#), courses and lectures that can help you develop your business idea.

Startup business grants from companies and nonprofits

Lots of corporations and large nonprofits, like the U.S. Chamber of Commerce, organize grant competitions. Some national opportunities include:

[iFundWomen](#). **iFundWomen** partners with other corporations to administer business grants. You can fill out a universal application to receive automatic notifications when you’re eligible to apply for a grant.

[Amber Grant for Women](#). **WomensNet** gives two \$10,000 Amber Grants each month and two \$25,000 grants annually. Filling out one application makes you eligible for all Amber Grants. To qualify, businesses must be at least 50% women-owned and based in the U.S. or Canada.

[National Association for the Self-Employed](#). Join NASE, and you can apply for quarterly Growth Grant opportunities. There are no time-in-business requirements for these grants of up to \$4,000, but you’ll need to provide details about how you plan to use the grant and how it will help your business grow.



FedEx Small Business Grant Contest. This annual competition awards grants to small-business owners in a variety of industries. You can [sign up to receive an email](#) when each application period opens. To be eligible, you'll need to have been selling your product or service for at least six months. Be mindful, though, that each grant cycle receives thousands of applications.

Fast Break for Small Business. This grant program is funded by LegalZoom, the NBA, WNBA and NBA G League and administered by Accion Opportunity Fund. You can win a \$10,000 business grant plus free LegalZoom services. Applications open during the NBA season, which runs from fall to early summer each year.

Minority Business Development Agency Centers. The MBDA, which is part of the U.S. Department of Commerce, operates small-business support centers similar to SBDCs. The MBDA doesn't give grants to businesses directly, but these centers can connect you with grant organizations, help you prepare applications and secure other types of [business financing](#).



WHAT'S YOUR FINANCIAL ID?

ARE YOU A GO-GETTER?

Finding the money to start a business and keep it going can seem like a huge obstacle. Just for fun, take the following quiz to see if you are a go-getter who can find funding. Write your answers on a separate sheet of paper.

1. I am willing to defer getting paid in order to see my vision succeed.

_____ Yes _____ No

2. I am willing to ask everyone I know if they want to invest in my enterprise.

_____ Yes _____ No

3. I am investigating every possibility I can think of for financing.

_____ Yes _____ No

4. I have spoken to at least one person who is a successful entrepreneur.

_____ Yes _____ No

5. I have the perseverance to reach my goals.

_____ Yes _____ No

6. My ideas are so clear that I can convince others to help me make them a reality.

_____ Yes _____ No

7. I am flexible and can readily adapt to change.

_____ Yes _____ No

Scoring:

The more "yes" answers you have, the more likely it will be that you will find funding.

Summary

- An entrepreneur is a person who takes the risk of starting a new business.
- Start-up costs include money for the purchase of assets needed to run a business, including inventory, equipment, furnishing, supplies, and utilities; costs such as legal, professional, and banking fees; licenses; permits; insurance; marketing costs; and remodeling and maintenance costs. Operating capital is the money needed to operate a business for the first few years. Reserve capital is money set aside for unexpected costs or opportunities.
- Sources of personal financing include personal assets, consumer loans, and home equity loans. Sources of private financing include family and friends.
- Some of the options available through bank funding are short- and long-term commercial loans, lines of credit, and secured and unsecured loans.
- The factors banks consider to approve commercial loans include the five C's: character, capacity, capital, collateral, and credit history.
- The Small Business Administration (SBA) is a major source of funding for new small businesses. This agency can also help with management training and organizational guidance.
- Other sources of funding for a business include business credit cards, private investors (angels), commercial finance companies, venture capital companies, and state and local agencies.

Communicating Key Terms

You are an entrepreneur talking with a bank loan officer about a Small Business Administration loan. Use as many of the terms below as you can to explain why the bank should give you a loan.

- | | | |
|-----------------------------|---------------------------------------|---|
| • entrepreneur | • line of credit | • private investor |
| • operating costs | • secured loan | • commercial finance company |
| • reserve fund | • unsecured loan | • venture capital firm |
| • private financing | • Small Business Administration (SBA) | • Small Business Investment Companies (SBICs) |
| • commercial debt financing | • LowDoc Program | |
| • commercial loan | • business credit card | |

Reference

Personal Savings

The first place to look for money is your own savings or equity. Personal resources can include profit-sharing or early retirement funds, real estate equity loans, or cash value insurance policies.

Life insurance policies

A standard feature of many whole life insurance policies is the owner's ability to borrow against the cash value of the policy. This does not include term insurance because it has no cash value. The money can be used for business needs. It takes about two years for a policy to accumulate sufficient cash value for borrowing. You may borrow most of the cash value of the policy. The loan will reduce the face value of the policy and, in the case of death, the loan has to be repaid before the beneficiaries of the policy receive any payment.

Home equity loans

A home equity loan is a loan backed by the value of the equity in your home. If your home is paid for, it can be used to generate funds from the entire value of your home. If your home has an existing mortgage, it can provide funds on the difference between the value of the house and the unpaid mortgage amount. For example, if your house is worth \$250,000 with an outstanding mortgage of \$160,000, you have \$90,000 in equity you can use as collateral for a home equity loan or line of credit. Some home equity loans are set up as a revolving credit line from which you can draw the amount needed at any time. The interest on a home equity loan is tax deductible.

Friends and Relatives

Founders of a start-up business may look to private financing sources such as parents or friends. It may be in the form of equity financing in which the friend or relative receives an ownership interest in the business. However, these investments should be made with the same formality that would be used with outside investors.

Venture Capital

Venture capital refers to financing that comes from companies or individuals in the business of investing in young, privately held businesses. They provide capital to young businesses in exchange for an ownership share of the business. Venture capital firms usually don't want to participate in the initial financing of a business unless the company has management with a proven track record. Generally, they prefer to invest in companies that have received significant equity investments from the founders and are already profitable. Venture capital investors also prefer businesses that have a competitive advantage or a strong value proposition in the form of a patent, a proven demand for the product, or a very special (and protectable) idea.

They often take a hands-on approach to their investments, requiring representation on the board of directors and sometimes the hiring of managers. Venture capital investors can provide valuable guidance and business advice. However, they are looking for substantial returns on their investments and their objectives may be at cross purposes with those of the founders. They are often focused on short-term gain. Venture capital firms are usually focused on creating an investment portfolio of businesses with high growth potential resulting in high rates of returns. These businesses are often high-risk investments. They may look for annual returns of 25–30% on their overall investment portfolio. Because these are usually high-risk business investments, they want investments with expected returns of 50% or more.

If some business investments will return 50% or more while others will fail, it is hoped that the overall portfolio will return 25–30%. More specifically, many venture capitalists subscribe to the 2-6-2 rule of thumb. This means that typically two investments will yield high returns, six will yield moderate returns (or just return their original investment), and two will fail.

Angel Investors

Angel investors are individuals and businesses that are interested in helping small businesses survive and grow. So their objective may be more than just focusing on economic returns. Although angel investors often have somewhat of a mission focus, they are still interested in profitability and security for their investment. So they may still make many of the same demands as a venture capitalist. Angel investors may be interested in the economic development of a specific geographic area in which they are located. Angel investors may focus on earlier stage financing and smaller financing amounts than venture capitalists.

Government Grants

Federal and state governments often have financial assistance in the form of grants or tax credits for start-up or expanding businesses.

Equity Offerings

In this situation, the business sells stock directly to the public. Depending on the circumstances, equity offerings can raise substantial amounts of funds. The structure of the offering can take many forms and requires careful oversight by the company's legal representative.

Initial Public Offerings

Initial Public Offerings (IPOs) are used when companies have profitable operations, management stability, and strong demand for their products or services. This generally doesn't happen until companies have been in business for several years. To get to this point, they usually will raise funds privately one or more times.

Warrants

Warrants are a special type of instrument used for long-term financing. They are useful for start-up companies to encourage investment by minimizing downside risk while providing upside potential. For example, warrants can be issued to management in a start-up company as part of the reimbursement package. A warrant is a security that grants the owner of the warrant the right to buy stock in the issuing company at a pre-determined (exercise) price at a future date (before a specified expiration date). Its value is the relationship of the market price of the stock to the purchase price (warrant price) of the stock. If the market price of the stock rises above the warrant price, the holder can exercise the warrant. This involves purchasing the stock at the warrant price. So, in this situation, the warrant provides the opportunity to purchase the stock at a price below current market price. If the current market price of the stock is below the warrant price, the warrant is worthless because exercising the warrant would be the same as buying the stock at a price higher than the current market price. So, the warrant is left to expire. Generally, warrants contain a specific date at which they expire if not exercised by that date.

Debt Financing

Debt financing involves borrowing funds from creditors with the stipulation of repaying the borrowed funds plus interest at a specified future time. For the creditors (those lending the funds to the business), the reward for providing the debt financing is the interest on the amount lent to the borrower. Debt financing may be secured or unsecured. Secured debt has collateral (a valuable asset which the lender can attach to satisfy the loan in case of default by the borrower). Conversely, unsecured debt does not have collateral and places the lender in a less secure position relative to repayment in case of default. Debt financing (loans) may be short-term or long term in their repayment schedules. Generally, short term debt is used to finance current activities such as operations while long-term debt is used to finance assets such as buildings and equipment.

Friends and Relatives

Founders of start-up businesses may look to private sources such as family and friends when starting a business. This may be in the form of debt capital at a low interest rate. However, if you borrow from relatives or friends, it should be done with the same formality as if it were borrowed from a commercial lender. This means creating and executing a formal loan document that includes the amount borrowed, the interest rate, specific repayment terms (based on the projected cash flow of the start-up business), and collateral in case of default.

Banks and Other Commercial Lenders

Banks and other commercial lenders are popular sources of business financing. Most lenders require a solid business plan, positive track record, and plenty of collateral. These are usually hard to come by for a start-up business. Once the business is underway and profit and loss statements, cash flow budgets, and net worth statements are provided, the company may be able to borrow additional funds. Commercial Finance Companies Commercial finance companies may be considered when the business is unable to secure financing from other commercial sources. These companies may be more willing to rely on the quality of the collateral to repay the loan than the track record or profit projections of your business. If the business does not have substantial personal assets or collateral, a commercial finance company may not be the best place to secure financing. Also, the cost of finance company money is usually higher than other commercial lenders.

Government Programs

Federal, state, and local governments have programs designed to assist the financing of new ventures and small businesses. The assistance is often in the form of a government guarantee of the repayment of a loan from a conventional lender. The guarantee provides the lender repayment assurance for a loan to a business that may have limited assets available for collateral. The best known sources are the Small Business Administration, www.sba.gov/ and USDA Rural Development, www.rd.usda.gov/.

Bonds

Bonds may be used to raise financing for a specific activity. They are a special type of debt financing because the debt instrument is issued by the company. Bonds are different from other debt financing instruments because the company specifies the interest rate and when the company will pay back the principal (maturity date). Also, the company does not have to make any payments on the principal (and may not make any interest payments) until the specified maturity date. The price paid for the bond at the time it is issued is called its face value. When a company issues a bond it guarantees to pay back the principal (face value) plus interest. From a financing perspective, issuing a bond offers the company the opportunity to access financing without having to pay it back until it has successfully applied the funds. The risk for the investor is that the company will default or go bankrupt before the maturity date. However, because bonds are a debt instrument, they are ahead of equity holders for company assets.

Lease

A lease is a method of obtaining the use of assets for the business without using debt or equity financing. It is a legal agreement between two parties that specifies the terms and conditions for the rental use of a tangible resource, such as a building or equipment. Lease payments are often due annually. The agreement is usually between the company and a leasing or financing organization and not directly between the company and the organization providing the assets. When the lease ends, the asset is returned to the owner, the lease is renewed, or the asset is purchased. A lease may have an advantage because it does not tie up funds from purchasing an asset. It is often compared to purchasing an asset with debt financing where the debt repayment is spread over a period of years. However, lease payments often come at the beginning of the year where debt payments come at the end of the year. So, the business may have more time to generate funds for debt payments, although a down payment is usually required at the beginning of the loan period.