Finance

In days past a handshake with your banker was all that it took to obtain financing to start a business or to obtain a loan for your existing business. In today's environment it can be very challenging to obtain any loan. The following is a list of ideas that may work for you and your business.

1. Get a Bank Loan

Because lending standards have tightened you will need a business plan and projected revenues and expenses for your new business and at least an executive summary and current financials if you have an existing business. Many lenders will use the SBA program to guarantee your loan and reduce the risk for the lender which will increase your chances of securing a loan.

2. Ask Family and Friends

There is no harm in asking; and family and friends may want to help. Make sure you treat this as business, show them a formal business plan and explain how you intend to pay them back. You need to tell them about the risks involved, how you will pay them back and secure the loan with a note. After all your family will always be there.

3. Check your 401 k

You may be able to tap into your 401 k without penalty. You will need to set up a corporation and someone with experience to set this up such as an attorney or CPA.

4. Credit Cards

You can use a credit card but this can be risky business. Pay the minimum monthly and it can take you years to pay this off. However used responsibly it can get you out of a jam.

5. Investors

There are investors out there and they look for certain types of business. They will want you to know your business. They too will want a business plan, financial information and market analysis.

6. Crowdfunding (non-equity)

For those of you who don't know this can be an effective way to raise money. There are several sights on line. Kickstarter and Indiegogo are the main ones. You set a goal for how much money you want to raise over a period of time. Your family, friends and strangers can then pledge money to your project using credit cards or pay pal. However on many of the sights if you don't reach your goal the funds are returned to the contributors and the sites do collect a fee for this.

7. Peer-to-Peer Lending

Also known as person-to-person lending and P2P lending, this is loans made by individuals to another individual without going through traditional financial institutions such as a bank. Often referred to as social lending, the loans are unsecured and interest rates are typically lower than a bank for the type of loan because of lower costs and lenders are competing on interest rates; but higher than would be received if the lender had it in a CD or money management account. There are also online platforms that charge a fee to facilitate the loan. This is a good option for high risk borrowers with little to no collateral who are seeking a micro-loan of less than $50k. The risk is that you don't know the lender nor the stability and security of the lending platform you use.

8. Factoring

Also known as accounts receivable financing, is one of the oldest methods of in-house financing. Factoring, simply put, is when a business sells its receivables to a financial institution or "factor". The factor will advance funds on a portion of the receivables, usually 75-80% of their face value. The remaining 20-25% is known as the "reserve" and is initially held by the factor. The amount of the reserve will vary with the quality of the receivables and the historical average of the payers. Historical late payers will increase the amount of the required reserve.

The factor handles the transactions, administers the accounts, conducts credit assessments and handles collections. For these services and the funds advance, the factoring costs to the borrower may exceed 20% of the face value of the receivables. Once the accounts are paid, the borrower receives the difference between the face value and the reserve. The factor usually gets a 2-3% fee.

The benefits of factoring include quick access to cash (usually within 10 days) and the fact that with a growing business, more accounts receivable will be coming in. The drawback is that it's expensive.

9. Convertible Debt

Convertible debt instruments are essentially asset-backed loans that can require the business owner to give up some future equity in the business if the lender wishes to convert the debt to an equity position in the company. One of the benefits is that the lender incurs less risk in making this type of loan and therefore is more likely to make the loan even with some risk in the situation. It is also less risky for the lender than a straight equity investment if the lender just wants to be paid back with a return and doesn't want ownership. This may occur if the company's bottom line growth is not performing as anticipated.

The dangers and drawbacks to the borrower are the potential loss of future equity if the company does well. Conversely, the owner may be required to pay back unconverted debt if the company is performing below budget.

Conclusions

Availability and choice of financing will be governed by the unique variables inherent in the needs, capacities and credit history of the borrowing business or individual. These will include timing requirements, asset bases, geographic location, risk tolerances and the ability to pitch the soundness and success potential of the business, among others. If thorough and competent credit market shopping and evaluation is done, you can get the financing you need.