10 Steps to Successful Business Financing

By Brian Madigan LL.B.

1 Right Lender

You will have to find the right lender for your business. This might be yourself, family, friends, business partners, former owners or institutional lenders. Remember that you can lend money to your own business and register security by way of a chattel mortgage. This option is not simply restricted to third parties. As for institutional lenders, many will have a great deal of experience with your particular type of business. Here, you can obtain expert advice for "free" as part of the financing. Take advantage of this opportunity and select the right lender. A good mortgage broker can help.

2 Vendor Take Back

The one single person with the greatest interest in your success could be the present owner. Who knows the business better? If the vendor agrees to assist you with the financing, then this will offer some credibility to the banks. Why? The banks will see that the vendor believes that you will be successful, and will help you if there is a difficulty. Further, the vendor who has yet to be paid will be an obvious purchaser, if you run into difficulty. It may be worthwhile to pay a little more in order to secure this financing.

3 Term

Long term and short term financing need to be combined and optimized. Finance the purchase price and possibly some of the working capital. The main reason businesses fail is that they simply run out of money. Deal with this issue upfront and ensure that you are properly financed. Equity financing is part of the overall equation and a lender will like to see that the new owner has some capital at risk.

4 Rates

Don't worry so much about the rates. Make sure that you have the proper lender and the proper repayment plan. Of course, the rates need to be fair, but going solely for the lowest quoted rate can be risky. Sometimes, this is simply a short term rate designed to get you in the door. In three months, you are back to paying the regular rates.

5 Payments

This is extremely important because this is your cash flow. The total gross dollars going out of the business each month will ultimately effect your success. As you grow, you can increase the principal repayments.

6 Valuations

What is the business worth? How much financing can you get? If an experienced lender will offer you the funding without collateral guarantees on the strength of the business alone, then, this is a good business. But, you have to ask yourself: how much could I sell this business for, if I needed to sell it in the next 3 months? That may give you a guideline as to how much you should be paying in the first place.

Some lenders are more flexible in terms of financing older, used equipment. Computers are notoriously worth less than their depreciated value on the books. But, specialized machinery may be worth more.

7 Guarantee

If you can avoid a personal guarantee, then do so. Remember not everyone you deal with will require a personal guarantee. Your objective, as your business grows, should be to eliminate any personal guarantees. Certain small business loans are government guaranteed, so your personal liability is limited to 25% of the loan. Watch this matter carefully.

8 Collateral

Obviously, you will have to pledge the assets of the business as security for repayment of the loan, but be cautious if your lender requires more. That usually means that the lender doesn't think the business is worth what you think it's worth. If you are asked to pledge your house, then reconsider the purchase. However, this is different from withdrawing equity from your house to put it into the business. That step may be wise, but incurring further unnecessary liability could prove foolhardy.

9 Acceleration of Debt

You will want to ensure that your banker can't simply walk-in and take over the business. And, if you can't make a payment, you want to make sure that your entire loan has not been called. In some cases, private lenders may be somewhat unforgiving. A late payment may accelerate the principal. Now, you have to refinance the entire business, not just find the money for one late payment. This

could cost thousands in refinancing and legal fees. So, deal with this matter upfront and have a line of credit that you can draw upon in an emergency.

10 Transferability

If you are going to sell you business, it would be helpful if your lender will continue with the new owner. The business arrangements are in place, and the best lender will be the one who knows the business. If your purchaser gets financing, then you can get paid. There may be a small approval fee, but the thousands of dollars required to put the security in place has already been paid. In fact, you paid it! If your purchaser doesn't have to pay it a second time, then he can afford to pay you more. Or, at least that's the theory. One way or the other, it's good to have this option available.

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