Funding Your Business

Money Makes the World Go Around

"A bank is a place that will lend you money if you can prove that you don't need it." —Bob Hope[1]

The Real Cause of Business Failure (Hint: It's not what you think)

Let's be honest about something and get this statement out of the way early: More than half of all businesses fail within five years.[2] Yep, there you go! It is on the table as a reality. Let's explore this in a little more detail. *Why* do most businesses fail?

Most say that it's because they were not adequately funded. You'll hear failed business owners say, *"We ran out of money."* Well, yeah—duh! Once the money is gone, the doors close. "*I ain't no quitter*" is a great trait for an entrepreneur, but if everything has been tried and the flaming writing on the wall says that the business is going to be insolvent (it can't pay its bills), sometimes quitting or selling is the cheapest way out of a bad situation. If an entrepreneur is in debt when the doors finally close, the show still isn't over because Guido the debt collector, and kneecap breaker, might still come a knockin'.

If you examine the postmortem of a failed business, however, you will find that the cause of death is rarely a lack of funding. The real cause is a lack of profitability, which is usually a reflection of poor planning, ineffective marketing, or a zillion other things (give or take a few). If they had saved up more money, they might have stayed open longer; but even with the necessary capital, without fixing the real problems, they would just be delaying the inevitable closure. If you have built a failing business, it doesn't matter whether you have a little cash or a lot of cash, the business will eventually fail, and the cash will be gone. It just depends how long it takes for the burning plane to crash.

The key is designing your business in such a way that it generates a quick profit so you don't burn through your cash. Make wise investments with the cash you have.

BIZ TIPS

Losing money is not always a bad thing. Depending on the type of business, the type of funding, and the income needs of the owners many business models plan to lose money in the beginning, maybe even for a few years. The key point to this section is not whether the business is losing money. The key point is whether the business is losing money unexpectedly without a solution to the problem. Unfortunately, most businesses that fail find themselves in this situation. Their business plans were inadequate.

A quick look into basic accounting will provide the most important financial equation of business ownership:

PROFIT = REVENUE - EXPENSES

Simply put, your business must quickly get more revenue (income) than expenses. There are two ways to increase profit. The first, obviously, is to increase revenue by making more sales or charging higher prices. There are many ways to do this, but making sales is relatively hard and raising prices can make sales even harder. Oftentimes, making a sale costs something. That cost might be in the form of advertising, discounts, supplies, employee time, or your personal time. You are in business to sell goods or services, and there are other chapters of this book that will help you maximize your opportunity to sell your goods or services. For now, the key here is that your business must bring in revenue quickly and on schedule. The failure to do this causes most business failures.

The second way to increase profit is to lower your expenses. This is, by far, the easiest way to increase profits—to a point. Uncontrollable expenses can quickly burn through your savings. Let's rephrase that last statement: unnecessary expenses can cause a business to fail. And to reiterate bluntly: If you're stupid in how you spend money, you'll be flipping that "We're Open" sign over to the "Sorry, We're Closed" side for the last time.

WARNING

Be careful about some business startup consultants who are quick to sell, or at least recommend, all kinds of unnecessary "get ready to do business" stuff. Depending on the type of business you're starting, you may not need a new computer system, multiline telephones, a website, an advertising campaign, a bookkeeper, fancy signage, custom pens, or even business cards. These expenses add up quickly, and using the equation of "Profit = Revenue – Expenses" you can be in the hole long before you make your first sale. It's exciting to buy lots of stuff ahead of time, but remember that most businesses fail because their expenses outweigh their revenue. Let's make a plan to earn some money before you go into unnecessary debt. This book has many fun and exciting start-up tools, but keep in mind the very important profit equation so your new business doesn't become a failure statistic.

Sharon, the owner of a copywriting business, uses an effective reward technique to help her manage her business expenses. She explains, "I budget really tight. No extras, bare bones. Yet I have a wish list of desired items for the business, all prioritized for purchase once I can afford them. When I have higher-than-expected revenue come in, I will use some of it to treat my company to something off the wish list. This is a nice morale booster." We all know that rash decisions can be made based on the current fire that is burning or the emotional need of the moment. Sharon's prewritten priority list helps keep her focused on what her next purchase should be.

AUTHOR SIDEBAR

When I opened our restaurant, I didn't budget for an expensive sign on the outside of the building. Luckily, our windows were large and we were able to apply high-quality vinyl decals of our logo and tagline. I decided I'd buy a big sign sometime down the road after we became profitable. However, I heard a growing amount of customer feedback about not being able to find our business while driving by. I realized that we really needed a sign, but it was just going to have to wait until I could safely afford it. I probably would have waited even longer if it had not been for a very good friend offering to loan me the money needed for the sign at a zero percent interest rate that I could pay back "whenever I was able to do so." I knew that was a gracious gift, and I paid him back in small increments over time.

Debt-Free Business Financing?

This next statement is going to be controversial, but it is often true for many types of businesses. In many cases, a well-planned business does *not* require years of saving, bank loans, or the sale of your offspring. Despite this, finances are often the reason people do not attempt to start a business, and they are often the reason most businesses fail.

ABC News shared excerpts from a *Good Morning America* interview with billionaire investor, Warren Buffett. Mr. Buffett is the CEO of Berkshire Hathaway. In that exclusive interview, the *Oracle from Omaha* shared some awesome quotes about going into debt (known as leveraging): [3]

> "Don't go into debt."
>
> "Stay away from leverage," he said. "Nobody ever goes broke that doesn't owe money."

> "A long, long time ago a friend said to me about leverage, 'If you're smart you don't need it, and if you're dumb, you got no business using it.'"

This chapter includes many different sources of funding, but the absolute, best kind of funding is the kind that doesn't put your business in debt. The section on bootstrapping will provide several ideas to demonstrate how creativity can significantly cut back on debt, or even eliminate it.

Figure Out What You Need

Potential Business Owner: "I'd like some help financing my new business. Can you help me?"
Loan Officer: "How much money are you going to need?"
Potential Business Owner: "I have no idea."
Loan Officer: (Delays responding because he is biting his lip to keep from laughing) "Well, how about a million dollars?"

Before you worry about where the financing is coming from, you first need to determine what you are going to need. Your financial needs will vary according to the type and size of your business. While financial needs depend on many different things, some generalities can be made. For example, production and processing businesses are usually capital intensive, requiring larger amounts of capital because of equipment, building size, and raw supplies needed. Retail businesses usually require less capital, and restaurants are somewhere in between. Of course, home based businesses usually provide the least financial requirements.

Start-up Costs Worksheet

The reality of new business ownership is that surprises are going to happen. Remembering that the easiest way to increase profit is to lower expenses, it's a smart idea to know as many of those expense costs as possible. The worksheet below will help give you a realistic idea of what your costs will be.

Here are some explanations of the three sections in the Start-up Costs worksheet below:

- Initial, One-time Costs: These are costs or portions of costs that are not repeated after the first year.

- Fixed Costs (Monthly): These are generally overhead costs that remain constant, regardless of the economic environment, your sales, or your payroll. If you have a fixed cost that is only paid annually instead of monthly, you will need to divide the annual charge by twelve to get the monthly charge required for this worksheet.
- Variable Costs (Monthly): These are flexible costs that rise and fall according to the economic environment, sales levels, or staffing. These can be more challenging to estimate, especially when you are guesstimating.

For example, let's say you buy office furniture for $5,000 which includes tax and interest charges. If you make a $1,000 down payment and then agree to pay off the $4,000 balance over the next three years, you'll only list $1,000 in the "Initial, One-time Costs," and the remaining $4,000 payments will be divided by 36 months to get $111.11 per month in the fixed cost section. If you haven't priced office furniture yet, it's time to do some window shopping so you can at least make some educated guesses.

Start-up Costs	**Essential? (Y/N)**	**TOTALS**
Initial, One-time Costs (costs that are not repeated in the first year)		
Building signage, A-frame signs, banners, window lettering		$
Business cards, letterhead, envelopes, uniforms		$
Business or franchise purchase price or down payment		$
Computers, printers, cabling, and related initial supplies		$
Formation fees (incorporation, business license, various permits and fees)		$
Furniture, fixtures, and equipment (paid in full or down payment)		$
Grand opening promotion, training costs		$

Legal and other professional fees		$
Operating cash		$
Setup/hookup fees or deposits for utilities, phone, cable service		$
Starting inventory, raw materials, parts		$
Tenant Improvement (TI), remodeling costs		$
Website development		$
Other		$
		$
TOTAL One-time Costs		$
Fixed Costs (Monthly)		
Advertising (yellow pages, Google AdWords, social media ads, etc.)		$
Furniture, equipment, hardware, software payments		$
Insurance, (liability, worker's comp, vehicle—not based on number of employees)		$
Lease/rent (building)		$
Loan payments (principal and interest)		$
Membership (chamber of commerce, industry dues)		$
Ongoing business/franchise payments (if not paid in full)		$
Telephone, internet, cable		$
Utility payments (if fixed, such as sewer or garbage)		$
Vehicle payments		$
Website hosting fees		$
Other		$
		$
TOTAL Fixed Costs (Monthly)		$
TOTAL Fixed Costs (6 months)		$
TOTAL Fixed Costs (12 months)		$

Variable Costs (Monthly)		
Accounting and/or bookkeeping services		$
Ad hoc advertising and marketing		$
Administrative costs (not part of payroll)		$
Insurance (health, life, disability, based on number of employees)		$
Inventory restocking, raw materials, parts		$
Office supplies (paper, inks, labels, etc.)		$
Payroll (including commission, bonuses, benefits, taxes)		$
Postage, shipping and handling		$
Salary draws of owner(s)		$
Telephone		$
Travel expenses		$
Utility payments (electric, water, gas)		$
Vehicle and major equipment costs (fuel, maintenance, repairs)		$
Other		$
		$
TOTAL Variable Costs (Monthly)		$
TOTAL Variable Costs (6 months)		$
TOTAL Variable Costs (12 months)		$
TOTAL STARTUP 6-Months (One-time + 6mo Fixed + 6mo Variable)		$
TOTAL STARTUP 12-Months (One-time + 12mo Fixed + 12mo Variable)		$
TOTAL STARTUP 24-Months (One-time + 24mo Fixed + 24mo Variable)		$

It's important to know these costs in order to know how much financing is needed. Not all segments of this worksheet will apply to all businesses. You will need to fill out a worksheet similar to this before deciding what kind and how much financing you need.

The real trick is trying to guesstimate what your revenues will be. In most but not all cases, a business will likely start selling product or services during the first year. This revenue will help offset the costs so you won't necessarily need all of that capital up front. For example, if you estimate that your first year's start-up costs will be $100,000, and you estimate that you'll sell $10,000 worth of goods or services in that first year, then the actual start-up costs will be $90,000. Figuring out exactly what your revenue will be is nothing short of a miracle in virtual time travel. When trying to determine your start-up figures, it is always a safer bet to overestimate costs and underestimate revenue.

SOURCES

To get more information or to download a free Microsoft Excel spreadsheet to help you calculate start-up costs, scan this barcode or go to www.HireSelf.com/business-financing

www.HireSelf.com/
business-financing

Figure Out What You Have (Your Net Worth)

"A wise man should have money in his head, but not in his heart."
—Jonathan Swift

Now that you have a fairly good idea of what kind of money you'll need, it's time to take an inventory of what you have.

The following is the basic formula you can use to determine your net worth:

NET WORTH = ASSETS - LIABILITIES

Net worth is the monetary value of an individual or a business. As demonstrated in the basic formula above, it is figured by subtracting the total dollar amount of all liabilities from the total dollar value of all assets. Net worth is simple to calculate if you are good at estimating. Unfortunately, estimating the true market value of some assets can be difficult. In addition, some assets might be carried on the books at their purchase price, instead of what they are worth today, which could be considerably more or less. Most value estimates are based on what assets could honestly sell for, not what you wish they could sell for.

The Net Worth worksheet below is a helpful place to start. Try to be conservative with your estimates. Estimate on the lower side of assets and the higher side of liabilities.

SOURCES

To get more information or to download a free Microsoft Excel spreadsheet that will perform the Net Worth calculations for you, scan this barcode or go to www.HireSelf.com/business-financing

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Net Worth	
Assets	**TOTALS**
TANGIBLE ASSETS (values, not amount owed)	$
Real estate residence sales value	$
Furnishings (sales value)	$
Owned rental real estate sales value	$
Vehicle sales value	$
Recreational vehicles (watercraft, RVs, plane)	$
Gold, silver, other precious metals	$
Art, jewelry, collectibles, musical instruments, and other valuables (Sales Value)	$

EQUITY ASSETS (value if sold or cashed out today)	$
Stocks	$
Insurance cash values	$
Variable annuities	$
Limited partnerships (sales value of your ownership share)	$
Other business interests (sales value of your ownership share)	$
FIXED PRINCIPAL ASSETS (include lower of cost or market value)	$
Fixed-dollar annuities	$
Trust deeds	$
FIXED-RATE ASSETS (include lower of cost or market value)	$
US government bonds and securities	$
Municipal bonds	$
Corporate bonds	$
Debt mutual funds	$
Face-amount certificates	$
CASH AND EQUIVALENTS	$
Savings accounts	$
Checking accounts	$
Money markets and cash reserve accounts	$
Certificates of deposit (CDs)	$
Under mattresses, buried coffee cans, piggy banks	$
Other assets that can be easily liquidated	$
TOTAL ASSETS	$

Liabilities (For amounts owed, include interest that will be owed as well, if significant)	**TOTALS**
Mortgage real estate residence	$
Owned rental real estate sales	$
Vehicle loan	$
Vehicle lease	$
Recreational vehicles (watercraft, RVs, plane)	$
Other items not paid off	$
Credit cards (total owed on all cards)	$
Personal debts (total owed)	$
Other Liabilities	$
TOTAL LIABILITIES	$
NET WORTH (= Total Assets – Total Liabilities)	$
If Net Worth is a negative number, then it's referred to as the Degree of Indebtedness	

If your Net Worth is actually a Degree of Indebtedness, meaning it's a negative number, you are likely in a bit of financial trouble. Sometimes there is a reasonable explanation for this and it can be temporary or fixable. For example, you might be upside down on your house but are deciding to continue to pay the mortgage because you love that house, can't refinance it, and feel the value will eventually go back up again. Also, many financially struggling people have started a business in order to pay off their debts and turn their financial life around. The key here is bootstrapping your business without a lot of personal financing or finding a financial backer that believes in your idea.

Sources of Start-up Funding

Now that you have a good idea how much funding you will need, you need to start putting together a plan for obtaining that funding. Most business owners end up combining an average of four or five of their sources together in order to obtain the capital to start their business. There are three key types of financing through which small businesses can get funding.

1. Equity financing is selling an ownership in your company.
2. Debt financing is a loan that must be paid back.
3. Lease financing is renting assets at a discount instead of buying them.

It is also helpful to plan *when* you'll need various amounts of funding. It's rare to need it all up front. Most of the time you'll be able to start out small as you grow your business from the ground up. This might include starting a side business and growing it as you can afford to grow it over time.

For example, Paul bootstrapped a small part-time printing business while working as a flooring salesman. He started in a spare room in his home with a nice laser printer he bought with a credit card. After a few months, he paid it off and decided he could afford to lease a higher-volume printer to add to his equipment. After a few more lucrative projects, he bought a paper cutter and automated folder using financing the seller offered. After a year, he bought several folding tables and an air ventilator as he moved into his garage so he could handle larger assembly processes. He obtained a micro-loan to purchase a large-scale banner printer and lease a high-performance offset printer for specialized projects. Using an equity loan, he leased and renovated a small, light-industrial shop with options to expand. He hired two employees and "fired" his flooring sales job to focus on his business full-time. After several years of excellent growth, Paul obtained a bank loan and bought a small abandoned warehouse with a small parking lot and shipping dock. He added 3-D printing to his services. Three years, two trucks, five high-tech printers, and twenty-two employees later, Paul is a dominant force in custom printing services for upstate New York, and his company has added several government printing contracts to its portfolio. Paul is now using some of his profits to act as an angel investor to help patent new printing technologies that he can use to further expand his business.

Paul is a great example of how to start and grow a business slowly and cautiously over time; however in some situations, a higher risk and larger chunk of money up front may be required. For example, Eric Fischer, the CEO of

JustBetterCars.com had to start his business by hitting the ground running. Luckily he had worked many years in the auto sales industry under some of the best teachers. He learned the skills needed and planned out his business carefully. It required a significant amount of capital up front in order to carry an expensive inventory of vehicles, a well-positioned property, and an attractive building.

The number of different ways you can finance your business provides a lot of flexibility for different situations. Hopefully you can avoid financing altogether, but when it's necessary to start or grow your business, it is nice to have options. Below is a fairly comprehensive list of financing opportunities for your business.

Personal Sources of Funding

You, Yourself, and You Too

Contributing your own assets to your own business is the easiest type of financing available. It doesn't require a promissory note, contract, sales pitch, or handshake. As long as your business is successful, you can eventually pay yourself back. There are a number of ways you can contribute to your own business. Some of these have more detail in sections further down in this chapter.

- Personal Savings can be contributed as equity or a loan to the business. In some cases, you can even have the company pay you back with interest. Be aware that in many cases entities you seek to borrow money from will want to know how much of a financial stake you have in the business. Their thoughts are along the lines of, "If he doesn't have enough faith in his business concept to put himself in some financial risk, why should we? He'll try harder to make it successful if he is invested too."

- Provide assets such as equipment, computers, software, furniture, office space, a vehicle, or supplies from your own personal assets. It's a nifty way to avoid the expense of purchasing them up front. Later, as the business revenue grows, the business can purchase replacements or buy them from you.

- Home equity line of credit. Draw from the value of your home.

- Sell (liquidate) personal assets for cash. This might include selling stocks, bonds, mutual funds, real estate, vehicles, or valuables.

- Borrow against your personal assets. Lenders might apply a lean against specific assets you possess and use them as collateral to back the loan. In the event that you default on the loan, this allows them to take possession of your collateral and sell it to gain back the balance of their loan.

- Many company retirement accounts and some life insurance policies allow the holder to borrow against the balance at a reasonable interest rate.

- Withdrawing early from retirement funds can be considered, but this is a very serious decision to make that can have dire results if you haven't replenished your fund when it comes time to retire.

- Withdraw cash out of insurance policies. To fulfill a dream some entrepreneurs without a young family or spouse to support justify cashing out their life insurance policies. This is a discussion that should not be taken lightly because your survivors may need that life insurance in the unfortunate event of your death.

- Start saving money. Set a portion of your revenue aside for the purpose of starting or growing your business. Depending on your sources of income, and how much you're willing to save instead of spend, you might be able to build up a nice little nest egg while you are planning out your new business.

Life Insurance Policies

Most whole life insurance policies allow you to borrow against the cash value of the policy and, with some policies, cash out a certain value from the policy. If it's a loan, you are essentially using your own money. It can be an easy way to get a loan or disbursement without having to put up collateral or jump through lending hoops to get qualified. There are no serious restrictions on what you can use this money towards, so business purposes are allowed.

If you borrow money from your policy, it is assumed that it will be paid back, but it is your money and you do not have to pay it back if you don't want to. You have to understand that the full value of the life insurance will not be paid out to your beneficiaries unless the loan is paid back. Because you are using money that you intended to leave to your beneficiaries, you might want to rethink your situation before making a decision. Also, you will lose the compounding interest effect on the money you've taken out of the policy, and it will reduce the payoff of the policy in the event you die.

This feature is not included in term life insurance policies because they have no cash value. For a whole life policy, it takes about two years for the policy to accumulate sufficient cash value for borrowing. If you've been paying into your life insurance policy for many years, there can be a significant nest egg of equity built up in the policy.

For many people whether or not to borrow from a whole life insurance policy comes down to answering a few questions:

- Are you far enough along in paying into your life insurance policy to have a sizeable nest egg available?
- Do you still need to leave a certain amount of money left to beneficiaries? In some cases, the children are no longer your dependents and have all grown and moved out. Your spouse might be gone (deceased, divorced), or is well positioned without your large policy.
- Does your dream of business ownership outweigh your desire to leave behind a nest egg for beneficiaries? Is there a compromise that you're willing to make?
- Should you talk this over with your beneficiaries and see if they are comfortable with a smaller payout in order for you to fund your business? Getting their support can help you sleep at night. In some cases, watching their reaction can help you decide as well.

Again, if there are extra funds available, while still being able to take care of loved ones, this money might be a blessing to use it to finance your business.

Home Equity Loan or Line of Credit

Home equity can be a source of significant funding for a business owner willing to borrow against the equity value in his home. The interest rates are often better than typical bank loan rates, and there is no requirement to prepare a business plan or sell your business concept to anyone. Approval depends on your income, credit scores, market value of your home, and the equity in your home (the difference between the resale value of your home and what you still owe on the mortgage). Mortgage loan officers will talk about the Loan-to-Value (LTV) of your home or property.

In most cases, when applying for home equity-backed financing, the lender will require that a full appraisal be performed on your home. Depending on the county in which you live and the amount of equity you have in the home, they might only require an Automated Valuation Model (AVM) that uses an automated formula based on recent sales of similar homes in the geographic area. The maximum amount that can be borrowed depends on these same factors and is usually limited to no more than 85 percent of the equity in your home, in case the housing market declines. Be aware that the required minimum LTV ratios can be different depending on the type of property (primary residence, rental, commercial) and the state in which it resides.

Unfortunately, it has become much more difficult to qualify for this type of financing because so many homes lost significant value, and the value hasn't recovered in many areas. For example, if a lender loans $80,000 on a fully paid home valued at $100,000 but the house goes upside down in a bad housing market, lowering its value to $70,000, the collateral of the house itself won't cover the loan. In this case, some homeowners relieve themselves of their financial obligations to their mortgage note by proceeding with bankruptcy, short sale, a deed in lieu of foreclosure, or just plain walking away from their properties. Because of the fallout from the recession, some lenders are still licking their wounds from the high percentage of bad equity financing deals they experienced. Government regulations have become stricter, requiring lenders to hold higher cash reserves, which has constrained all types of lending, including home equity loans and lines of credit. When you combine these factors together, it is clear that lenders are going to be a lot more conservative when it comes to equity-based lending.

Home equity financing can be set up as either a home equity loan (HELOAN) or a home equity line of credit (HELOC). A home equity loan is for a specific amount of money that you'll receive upfront. You'll repay the loan through monthly payments over a fixed term, much like your original mortgage. If you don't repay the loan as agreed, your lender can foreclose on your home. Unless your business really does need all of the money up front, it is often wise to consider an equity line of credit first because they are much more flexible.

A HELOC provides a source of funds that you can draw on as needed. You will be required to pay at least monthly interest payments to your lender, but repayment of the principal is usually up to you. If you can't start paying the principal back for a few years as you wait for your business to ramp up, no problem. The lender profits from the interest and doesn't mind if you take your time to pay back the principal so long as they get to keep collecting the interest. They know your house is the ultimate collateral if you are unable to pay for some reason. Any principal that is paid gets credited back to your equity value.

Often the interest is an adjustable rate set on a monthly basis as per either the national prime interest rate, or from a formula using other indexes. You might want to ask your lender ahead of time, which index it follows so you can follow along when you're bored. The interest that you pay on a home equity loan or credit line is tax deductible.

SOURCES

Home equity financing can be an excellent option for entrepreneurs, but these are big decisions that will require you to do some homework and talk to providers about the most current options. For more information about how home equity financing works (equity loans, equity lines of credit, and cash out refi's), including examples and a list of quality home equity financing providers, scan this barcode or go to www.HireSelf.com/business-financing

www.HireSelf.com/crowdfunding

Refinancing Your Home or Property

Refinancing your home, rental property, or other high-valued property on which you are making payments towards a loan might be a very good option for entrepreneurs wanting cash to use towards their business. This process is sometimes called a "cash out refi." The general concept is simple enough: take out a new loan and use it to pay off your old loan, thus essentially swapping a new mortgage for an old one. In order to take out cash from the deal, you will need to do one or both of the following:

1. Take out a new mortgage with a balance larger than the mortgage you are currently paying off, thus taking out some of the equity you've built up in the property. See the example below.

2. Qualify for a lower interest rate on a new mortgage compared to the interest rate on the old mortgage. This will save significant money over many years, and will let you to cash out on this savings. Interest rates can be lower if the nation's prime interest rate has dropped since you took the first loan, or if your own credit rating has significantly improved over the years, as generally happens when people financially mature by earning more income and accumulating a positive payment record over the years.

There are restrictions to the amount of equity in your home that can be pulled out. These restrictions consider your credit score and the total equity you have in the property. They also build in a safety factor for fluctuating property values that won't allow you to use more than 80% (for example) of the total equity value. This is a lot easier to do when interest rates are dropping, and you can often both lower your monthly payment and pull out a nice wad of cash in the process. For many entrepreneurs, obtaining the cash is sometimes worth it even if the monthly mortgage payment goes up a little in the process.

For a very simplified example (ignoring fees, interest, taxes), suppose your original mortgage loan was for $200,000. Over many years, we'll suppose that you have faithfully paid off $120,000 of your mortgage principle, thus leaving you with a balance owed of $80,000 ($200K-$120K=$80K). In the meantime, the resale value of your house has increased to $250,000, thus adding an additional $50,000 of equity value to your home. If you sold your home today for $250,000 and used the money to pay off your mortgage balance, you'd walk away with $170,000 in your pocket ($250K-$80K=$170K). Instead of selling your home, you can chose to refinance it and withdraw the equity. Let's say you qualify for a second mortgage loan for $150,000. The first thing you do is pay off the balance of your $80,000 first mortgage, thus leaving you with a theoretical $70,000 to cash out and use towards whatever you want (e.g., your business). The downside is that you still have to pay off the $150,000 second mortgage loan, often for the next 20 or 30 years. The upside is that the money you take out is tax-free in most situations. Talk to a trusted mortgage loan officer to see if you're a good candidate for a refi and to compare possible options for your specific situation.

Wills, Trusts, Early Inheritance, and Gifts

Sisters Gina, Juliet, Elisa, and Patricia spent eight years trying to get the right financing to start their dream business together. They met with banks, private investors, friends, and even an investment company that ended up stealing $30,000 from them before getting shut down because of fraud. They saved and tried to obtain additional funds but could not put together enough funding to start. Their parents were very supportive and kept encouraging them to keep trying. Not long after their father lost his battle to brain cancer, their mother invited them over and said that it was their father's wish to give his life insurance to them. This inheritance allowed these ladies to finally open the Four Sisters Cafe, and it has won multiple awards since.

One source of funding that often is a tremendous catalyst for business start-ups is the financial gift of someone close to the entrepreneur. It can be a trust account that is being paid, a will that is being paid out because of a death, or a financial gift that is being offered. In some cases, having friends who are willing to let you to live in their spare room for a while to help cut start-up expenses is an excellent boon for entrepreneurs. You might even have friends willing to provide a spare office, vehicle, or equipment.

Family and close friends might be more willing to help than you think. It is critical, however, that you do not expect or demand their help. Your relationship is far more important than any business deal. Before asking a family angel to provide you with a substantial amount of money through an early inheritance, a financial gift, or the sale of a valuable possession, you should lay out a plan and proceed cautiously. It is usually a good idea to first share your excitement and ask if they'd like to hear about your idea. Unless your timing is lousy, most family and friends would love to hear about your dream. In many cases, you should prepare at least a simplified business plan and, when the timing is right, walk them through it so you can educate them about your business idea. This helps them feel assured that you are serious and not just that wild-eyed teenager they remember from a few years back. Show them that you have passion about this business concept and that you have put a lot of work into designing it. As long as you don't sound like a used car salesman, your efforts to educate them should help them feel confident in your abilities.

As long as you laid out your plan and your financial needs clearly, it might be enough of a hint to get them to offer to help. If they don't offer, you have a choice to make, and only you can make that choice. A diehard salesperson would tell you to ask them for a specific amount and not to underestimate what they can give. As long as you clearly know they can easily afford the requested amount and you feel like they've been very receptive to your presentation, this might be a good approach. If you are concerned that they might not be on board or you are concerned about hurting your relationship, then going for a "hard ask" probably isn't your best option and you might have to back off on the pressure.

Let's assume that you only need $25,000 more for your venture and you are certain they can easily provide it as a gift, if they desire to help. Here is a list of possible statements you might consider using alone, or in combination with each other, depending on your situation:

- "Of the total start-up costs I've shown you, I think I can pull together funding (tell them how much) from my savings and by obtaining loans, but I'm still short $25,000 to make this business a reality."
- "I'd like to ask you if you'd consider gifting me the balance because I'm your favorite [child/nephew/neighbor/parent/barber]."
- "I know you said that you were going to leave your [valuable, non-family heirloom item] to me in your will, but I was curious if you'd ever consider [refinancing/selling/giving] it before you passed away. That way you could help me get my dream off the ground while you're still alive to witness it." Okay, well, this is going to take a lot of personalization to make it not sound so cheesy and insensitive!
- "Do you know anyone who might be willing to help me make this a reality, or would you personally be willing to help?"
- "Since you don't seem comfortable gifting the start-up funds, would you consider loaning it?"
- "I only married your daughter out of pity and now that we're divorced, it's the least you can do for ruining my life. Besides, if I have my own business, I won't have to make her pay alimony to me."
- "I raised you as my child for over twenty years, and I've changed over 3,000 of your diapers, taught you, coached your sports, attended all your events, helped you get a college degree, and paid for your wedding. This is something you can do for me." If the answer is "No." then you might add, "I guess I can always rewrite my will and give all of my assets to charity. Did you know you had a sister named Charity?"

If they do not offer it as a gift, they might be a solid source for a loan, and possibly a low or no interest loan with a very relaxed payback schedule (e.g., maybe you don't have to start paying back the loan for five years). Asking for a loan is obviously a fallback. In some situations, they might forgive the loan after that amount of time, but don't count on that grace, and definitely plan to pay it back as agreed. Remember that relationships are more important than money.

Sources of External Loans

External loans involve borrowing from resources that are not your own assets. This type of borrowing is known as debt financing. Debt financing involves borrowing funds from creditors (lenders) with the agreement that you'll pay it back at a future specified time, often through payments, plus interest. The benefit to you is that you'll get funding capital that you wouldn't otherwise have to launch your business or raise to the next level of expansion. The benefit to your creditors is that they earn more back than they loaned you because you'll pay a certain interest rate added to the principal loan amount that you borrowed.

Debt financing may be secured or unsecured. Secured debt requires collateral which provides the creditor with some security in the event you default on the loan. Collateral is a valuable asset that you or a cosigner will offer as a guarantee in the event you cannot pay back the loan. Should this occur, the creditor could take ownership of the collateral as payoff for the remainder of the loan.

Debt financing can be classified as short term or long term in the repayment schedules. Short-term debt is used to finance important business operations which might include things like raw materials, ramping up inventory for the holidays, or new signage. Long-term debt is used to finance major assets such as buildings and large equipment.

Eric Fischer, CEO of JustBetterCars.com, provides valuable insight regarding how to obtain external financing:

> "It's a challenge to get financing without matching collateral. In the past you needed to have a good reputation, be educated, have good credit, and a have a great story. It was about your relationships, your credibility, and your story. However, our legislators' good intentions have tied the hands of lenders that used to be able to lend money on a hunch, a good story, or a history of success without equity. If you are smart, your new relationships better get attached to the people who have already made it and have the cash you need. This may include giving up part of your company or even controlling interest of your growing company."

The Bank of Friends and Family

A common form of private financing comes from parents, siblings, grandparents, children, and other relatives or good friends who trust you or owe you a favor. These loans can be either debt financing or equity financing depending on what they are hoping to get out of the arrangement.

“*Friends and acquaintances are the surest passport to fortune.*” —Arthur Schopenhauer

The Bank of Friends and Family is not limited to loaning money. Borrowing assets like equipment, furniture, office space, a delivery truck, or supplies can result in huge savings until the business is able to purchase replacements or buy them from your family or friends.

Most entrepreneurs have shared their dream of starting a business with family, friends, and their network of social circles. In these various groups, there is a good chance that someone loves your enthusiasm and respects your abilities. This is also a valuable group to approach for leads to other people who might be able to provide financing or professional services. It is also a good group to use for a crowdfunding campaign. Don’t forget that these circles will be your initial group of potential customers and word-of-mouth marketers.

WARNING

It is highly recommended that you handle private financing sources with most of the same formality that would be used with outside lenders. This includes drawing up a contract that is clear about the terms of the loan or specifics of the equity investment. There are countless stories of families and friendships being ripped apart when a business fails or succeeds beyond expectations if the terms of the deal were made over a handshake. Not paying back Grandma might not only anger Grandma, but it also might alienate you from the rest of the family if they feel you took unfair advantage of her. If you are comfortable with this potential risk, the Bank of Friends and Family can be a great source of funding.

Banks

Although banks are popular sources for business financing, they can be one of the most frustrating places for a poor entrepreneur to seek financial assistance. Banks do make many loans to businesses, but banks are not much for risk taking, at least not anymore. If they are turning away families that want to buy a house to live in, but who have bad credit, what do you think they are going to say to a wild-eyed entrepreneur, with no experience or track record, who wants a large loan to start up a widget factory?

Banks are often not interested in loaning small amounts of money because the paperwork is, honestly, often more trouble than it's worth. You have to understand that banks get asked to loan money all the time, and they, like any business, need to make an efficient profit on those loans. Drawing up loan documents, doing credit checks, securing collateral, and other procedures has a definite cost, but it doesn't cost much more to put together a $150,000 loan than it costs to put together a $1,500 loan. However, if the bank were earning a flat 10 percent interest on the loans, they'd make $15,000 with the first loan and only $150 with the smaller loan, which is likely much more than the cost of putting together the loan. This is why most banks have a minimum loan amount.

The upside to a bank loan is that they provide short-, mid-, or long-term financing, and they can finance all of your needs, including equipment, real estate, capital for raw materials, or inventory. They will also allow you to pay off your loan early and terminate the agreement, whereas venture capitalists or other investors might not be so amenable.

If you, as a potential business owner, approach a bank, you must have reasonable expectations. The bank wants proof that you have a very good chance of being able to repay the loan. Expect to be asked for a solid business plan, history of a great financial track record, a résumé (to prove your experience and education), and personal assets to be used as collateral to back up a loan. If you don't have enough collateral, you'll need a guarantor or cosigner who satisfies the lender. It's sad but, you almost need to prove that you really don't need a loan in order to obtain a loan.

Most banks also require that you have a track record of success (see *The Five C's of Credit* below). If you haven't been in business for more than a couple of years, or you don't have vast expertise in the business for which you're trying to get a loan, don't expect to get a bank loan. That's why a start-up company often has a difficult time with banks.

When your business is humming and you want to expand or purchase a new piece of equipment, a solid track record shown with profit and loss statements, cash flow budgets, and net worth statements might allow you to borrow from a bank to jump to the next level.

The Five C's of Credit, or is that the Six C's of Credit? Proof of your creditworthiness to most banks and other professional lenders is determined by five (or six) critical factors:

1. Character (integrity): Character is not only the general impression you make on the prospective lender or investor, it is also the educational background and business experience in your industry that you and your team bring to the borrowing table. It is possible that a background check will be done, and you might be asked for references, both personal and professional. If you were convicted of fraud or theft, you might consider developing a partnership and letting your partner do the primary borrowing because it will take a very convincing story to convince a bank to trust you. They will check your credit rating and might even ask for educational transcripts. Don't be dishonest. Understand that there is a certain amount of subjectivity on the part of the lender who sits across the desk from you. If you don't impress them as trustworthy, honest, and even likeable, it's easy for them to find reasons to deny your loan.

2. Capacity (sufficient cash flow to pay back the loan): Your capacity to repay is probably the most important of the five factors. Potential lenders need to know exactly how you will repay the loan. They'll want to consider the cash flow from the business in relation to the timing of the payment schedule. They'll need to determine the probability that you can successfully pay off the loan in relation to other existing credit relationships you have. Your track record for successfully paying off debts will be an indicator of future payment performance. They'll want to know what other possible sources of repayment exist in the event your business doesn't succeed as expected. Also, in most cases, every principal who owns more than 10 percent of the company will be required to sign a personal guarantee for the debt.

3. Capital (net worth): This is the money you personally have invested in the business and is a good indication of how much you have risked in the event of a business failure. Many lenders want to see you invest around 25 percent of the funding. Lenders and investors want to see that you have risked a personal financial stake in the business

before you asked them to commit funding. It gives them comfort knowing that you will work harder to ensure the business is successful to protect your own investment. Be careful, though, because if you commit too many of your own assets, you might not have enough collateral left to get a loan.

4. Collateral (assets to secure the debt): Collateral is a guaranteed pledge of an asset you own, such as your car or real estate, that a lender can use as a source of payment in case you can't repay the loan. It's like laying your car keys down in a game of poker when you don't have the cash to back up the bid. If you lose that hand (your business doesn't succeed), you're walking home. Lenders want things that have a deed or a pink slip because they can put a lean on those items preventing them from being sold until the loan is paid off. Lenders do not like repossessing items because it's bad for business, and these assets are harder to liquidate. In some cases, a business can use accounts receivable, inventory, and major equipment as collateral, but these are not preferable because of the difficulty in liquidating them.
   Another form of collateral is a guarantee from another party. Guarantees are essentially cosigners who also sign a guarantee document promising to repay the loan if you can't. Some lenders may require a guarantee in addition to collateral as security for a loan.

5. Conditions (of the borrower and the overall economy and the situation at hand): Conditions include the intended purpose of the loan, whether it will be used for working capital, additional equipment, inventory, or to pay off another loan. The lender will consider local economic conditions and trends in your industry as well as in industries that supply you or buy from you.

6. Some experts have included a *Sixth C*, but it's funny that they don't all agree on what that "C" is. Some say it's insurance *Coverage*, which is important, yet not all lenders ask for proof of coverage. Others say it's *Common Sense*, meaning your ability to make wise financial decisions, but this is really covered under Character. Most who add a Sixth C, tend to add *Confidence* to the list. Although Confidence seems like it would be covered under Character, the way confidence is typically used seems to fit as a sixth item: a potential borrower can instill confidence in a lender by addressing all of the lender's concerns on the other Five C's. Their loan application sends the message that the company and the borrower is professional, well organized, and conveys that they have what it takes to be successful and that they will easily pay back the loan.

Commercial Finance Companies

Commercial finance companies are an option when a business is unable to secure financing from other commercial sources. These companies are usually more willing to rely on your collateral than on your financial history or success projections for your business. Because finance companies take on higher risks, the interest payments for these types of loans are usually higher than commercial lenders.

BIZ TIPS

Do your homework and don't rush. Anytime you decide that you'll have to borrow money, ask around for lender recommendations. Shop around and compare rates, but don't forget to ask about fees and other conditions. Talk with banks, savings and loans, credit unions, mortgage companies, and mortgage brokers. Ask all the lenders you interview to explain the loan plans available to you. You need to know and understand more than just the monthly payment or the interest rate. If you don't understand loan terms and conditions, ask questions. Remember, the stupid questions are usually the ones never asked. Not doing your homework might mean higher costs or stricter terms than you might have had otherwise.

Credit Cards

As expensive as this might be, credit cards are a common form of business financing. The interest rates are usually high, but you don't have to present a business plan or provide collateral in order to use them. Credit cards are especially useful as simple microloans when new equipment is needed or for emergency expenditures when you know you can pay it off fairly soon without carrying the balance for too long.

Because the interest rates tend to be high for credit cards, they are very expensive if you use them for long-term financing. Shop around for zero percent (or low) interest credit cards. These are especially useful for emergency purchases if you don't have the cash to back it up, but can pay it off in six months or whenever the special interest rate ends. Do not forget to mark your calendar with the date the interest kicks in, because it's usually a pretty high rate. Understand that there is a reason these companies offer special, low or no interest rates. The credit card companies are not stupid. They know that undisciplined people will often wait and try to pay it all off later when they should, instead, break the price down into affordable chunks and start paying it off early. These companies know that if you can't pay for the total price of the item now and had to use your credit card to make the purchase, you probably won't be able to pay the total price for the item later. Then they'll collect their interest at that time as you then start making payments.

As an example, let's say you pay for a $6,000 piece of equipment on a promo credit card that gives you six months of zero percent interest but jumps to twenty-five percent interest on month seven. When you make the purchase, you should budget yourself to make six payments of $1,000 each so you can have it paid off before that seventh month arrives. The good news is that you'll have up to a month to pay the first payment of $1,000, depending on when your bill arrives. Because the rules can be tricky in regard to exact dates, it might even be wiser to plan on paying it off in five monthly payments of $1,200 each so you don't accidently cross the expensive line into interest penalties.

BIZ TIPS

For many business owners with stable businesses, credit cards often provide a nice perk. For example, many cards provide frequent-flier miles, hotel credits, cash back, and many other perks. Many business owners, especially sole-proprietors, try to use their business's credit card for all business-related purchases with the habit of paying off the entire credit card bill each month when the statement arrives (or set it up for auto pay). This way they can maximize the perks without ever paying any interest. Sole proprietors later use these perks for personal vacations or similar nice side effects. LLCs and corporations with a corporate card can be selective in the type of card they use and can roll the perks into business savings, discounts, or benefits.

Small Business Administration

The Small Business Administration (SBA) offers multiple loan programs to small businesses that are not able to obtain reasonable financing through traditional channels. For example, the *7(a) Loan Guaranty Program* allows banks to offer small businesses loans that are guaranteed by the SBA up to a very large percentage of the loan. This removes most of the risk from the bank if the loan goes into default. The small business owner isn't completely off the hook because the bank will come after its non-guaranteed portion of the loan, but the risk is lower than putting your home up as collateral. See the section on Microloans below. Check out the SBA's website (www.sba.gov) for more information.

BIZ TIPS

Shop around for SBA loans since there are usually multiple lenders offering them. Some banks make extra money by selling the guaranteed portion of the loan to pension funds and insurance companies in order to collect service fees and quick profits. In these cases, you might be able to find a lender with lower rates than others.

Small Business Investment Centers

Small Business Investment Centers (SBICs) are usually privately owned investment companies that provide funding for startups and small business needs. SBICs are licensed and regulated by the SBA, which can often provide you with a list of SBICs.

These organizations can provide enticingly low interest rates when lending alongside a bank. If you're able to get into one of their programs, here is an example of how it might be used: say that you need to put together funding for a $200,000 building. A bank might offer a loan of $150,000 with a variable interest rate, leaving you with $50,000 left to fund. A SBIC might be willing to come in with a $25,000 second mortgage and an even lower fixed-interest rate without all the points and fees that the bank might charge. Often the SBIC will offer extended terms, so you only have to pay interest for the first few years until you can get your cash flow going. Sometimes they will even delay your first payment for several months while you get your business started.

Microloans

A microloan is helpful for startups and businesses. They are easier to obtain than a bank loan, especially if you're just outside of the bank's requirements. Microloans are great for startups, whereas banks won't look at most start-ups.

The SBA provides funds to specific types of intermediary, nonprofit community-based organizations to, in turn, loan to eligible borrowers. Believe it or not, the USDA (yep, the United States Department of Agriculture) is a big funder to intermediaries for the purpose of helping rural, agriculture-related businesses.

Most microloan programs provide loans between $1,000 and $50,000 to help small businesses start up or expand. The USDA can loan up to $150,000 in population-sensitive areas. The average microloan is around $12,000.

The intermediaries are often connected to economic development districts in large cities, counties, or groups of counties. The districts that have intermediary lenders compete against other intermediaries for available federal funding by demonstrating how their regional demographics fill a particular niche the government wants to fill (e.g., low income areas, agriculture, areas with high unemployment, etc.). Intermediaries fund their programs by charging borrowers a higher interest than they pay to borrow the funds. Because the intermediaries have to pay back the loans to the SBA and USDA, they usually require collateral from the borrowing business or cosigners to insure they get their investment returned.

Another advantage of intermediary microloans is that they are typically fixed-rate loans, while banks usually charge variable-rate loans. Bank loans usually start with a lower interest rate but as interest rates grow, they can quickly pass up fixed rates, and many variable rate loans don't have a ceiling. Intermediaries do not have a prepayment penalty, meaning that if you can pay it off faster than scheduled, you won't be penalized. Banks often invoke a three-year prepayment penalty so they can assure themselves a certain level of interest profit. Unlike banks, intermediaries don't sell your loan to a secondary market. An average payback for an SBA microloan is about six years, while a USDA microloan is thirty years, although some intermediaries require terms of twenty-five years or less.

In some situations, microloan intermediaries might require any of the following before a loan can be considered. Understand that it depends on the intermediary. Because the requirements vary widely, be sure to check with your regional intermediary to find out if they require any extra hoops for your jumping journey.

- Business management classes: These training programs help increase the likelihood of business success, thus increasing the chances of the business being able to pay off the microloan. This can be a helpful requirement for a business owner who needs it but can be annoying for an experienced owner who doesn't. Again, not all intermediaries require this. The requirement can be situational so be sure to ask before you're surprised.

- Business plan: Many intermediaries require that potential borrowers have a business plan with projected income figures that stretch out a few years. The business plan should contain major segments including market research.

- Personal tax returns: These establish your past income history and can illustrate a pattern of stability.

- Credit score: The intermediary will often pull these scores for you upon receiving a completed loan package. Colleen Crowden, Loan program Supervisor at Sierra Economic Development District, explains, "Your credit score can raise big red flags. If a potential borrower has challenged credit, it is generally not good. It shows an unwillingness to pay bills. If a bankruptcy is involved or there are other derogatory items within the report, it can be forgivable depending on the reasons that caused it, and supporting documentation for the explanation. A borrower's record of excellent payment responsibility after the bankruptcy is imperative to acquire credit at a reasonable rate."[4]

- Personal résumé: Showing past job history helps demonstrate prior skills and experience that support your potential success at running this business. If you have a strong history of working in the restaurant industry, including successful management of a restaurant, it helps support that you have what it takes to manage your own restaurant. If you've never worked in a restaurant and your only experience is eating in a restaurant, however, you might be in for some serious challenges if you try to open your own steak house.

Intermediaries value new businesses with a strong potential for job creation. Spurring job creation is a major motivation behind the government's microloans to many intermediaries. When an intermediary is trying to decide whether you are a good candidate to receive specialized loans, it is critical that you can demonstrate your ability to repay the loan and that you are a good addition to the region because of the potential employment opportunities you offer or the service segment you fill. They have some flexibility in selecting loan recipients, so do your homework and be impressive.

SOURCES

To find the closest Small Business Administration (SBA) District Office, you can scan this barcode or go to www.HireSelf.com/business-financing

www.HireSelf.com/
business-financing

Government Grants and Loans

Federal, state, and local governments offer special grant programs and low-interest loan programs to encourage specific types of business growth, depending on the government's desires. These government-sponsored programs might specifically target:

- Industries and business segments in which the government wants to see development or growth. If the federal government wants to decrease their reliance on fossil fuels, they might offer grants and low-interest loans to businesses focused on alternative energy to encourage and faster growth in this particular business segment. Other examples of business segments include scientific research and development, certain agricultural trades, healthcare, transportation, weaponry and defense segments, space, numerous technology trades, communication systems, and many more.

- Certain categories of business owners, such as military veterans, women, minorities, senior citizens, young adults, single parents, and numerous other types and combinations of these types.

- Geographic locations that typically relate to economically disadvantaged communities or areas in which the government wants to see growth. Examples might include inner cities and impoverished areas, communities ravaged by natural disasters, closed military bases, service areas near newly developed highways, or a shopping center in the middle of a newly developed neighborhood.

Because tax dollars fund government grants, they have very strict compliance requirements and sometimes require insane amounts of documentation to ensure the recipient is using the funds as specified.

Peer-to-Peer Lending Sites

A recent trend in the past few years is peer-to-peer (P2P) lending websites. P2P sites offer opportunities for creditworthy business people to seek out funding from individual or institutional investors.

You can apply for a loan through these websites. Investors who are registered with the P2P sites can review your application and decide whether or not they wish to fund your proposed business through interest-based loans. These P2P sites are online alternatives to traditional lending institutions and are expected to grow as quick, confidential sources for start-up funding. Borrowers with good credit can get the best interest rates on unsecured loans without all the red tape and fees associated with traditional banks and lenders. The key is your credit score, and it has to be strong.

SOURCES

Peer-to-Peer (P2P) sites vary in functionality and focus. For an updated list of P2P sites, scan this barcode or go to www.HireSelf.com/business-financing

www.HireSelf.com/business-financing

Private Placement

A private placement is a special offering of either stock or debt. It is the opposite of a public offering. The placement is offered to select investors such as wealthy individuals, large banks, mutual funds, insurance companies, pension funds, or venture capital firms without going public. If debt is being offered, it's treated much like a specialized loan. Private placements are often a cheaper source of capital than a public offering because it doesn't have to be registered with the Securities and Exchange Commission, and detailed financial information is not disclosed.

Bonds

Bonds are a specialized form of debt financing used to raise funds for a specific activity. The business issues the bond, the debt instrument. Bonds are different from other debt-financing instruments because the business specifies the price (the face value), interest rate, and the maturity date (the date the company will pay the investor). The trick is making it appealing enough for investors but realistic enough for the business to be capable of paying it back. The benefit to the business is that it doesn't have to make any payments on the principal, and it can choose ahead of time whether or not to make any interest payments until the specified maturity date. This means the business gets to apply the full value of the financing towards the specific activity for which it borrowed the money. The investor risks the business defaulting on the bond or filing for bankruptcy. Because bonds are debt instruments, however, they rank higher than other equity holders when liquidating assets.

Vendors and Suppliers

Vendors who see value in your business might be interested in helping you finance it. Dick Schulze, the founder of Best Buy, used financing from his vendors to stay afloat in the early days.[5] Your vendors might have a vested interest in your success, especially if you are a key supplier for them.

Loan Sharks and Guido the Kneecap Breaker

Loan sharks are predatory lenders and definitely in the carnivore family. They might loan money when more formal institutions won't, but the interest rate on this loan often reflects the high risk they are taking in issuing that loan. These folks don't call themselves loan sharks, it's a term applied to them because they feed off the weak and desperate. You can find some of their ads in the back of newspapers and local magazines. They are the private lenders with big interest rates, but low thresholds of acceptance. Some of these folks are ethical and reputable, but the loan sharks in this section are not necessarily ethical and reputable when it comes to collecting payments.

Some of these lenders are formal and require paperwork that enables them to take possession of your assets to repay a defaulted loan in the event that you don't pay it back as specified. When your meeting with a loan shark raises the hair on the back of your neck and resembles anything like what you see in gangster movies, turn around and run.

Loan sharks have the reputation of getting repayment by whatever means necessary. Blackmail and threats are by-products of some loan sharks. Worrying about a visit from Guido the Kneecap Breaker is something that will keep you awake at night in the event your business ventures turn south. Seriously, if you find yourself tempted to approach a loan shark for funding, you really need to consider if it is a good time to start your business. Otherwise, you better have one heck of a great business plan that will ensure you will be successful, because you don't want to open your door and find Guido smiling at you with a baseball bat resting over his shoulder.

Sources of Investors

Business Equity Financing Partners

Equity financing is the process of trading a portion of the ownership in the business for a financial investment in the business. This is not a loan to be repaid at a later date; it is an actual, permanent partial ownership of the business.

This new equity partner can be active in running the business or just be a passive investor who believes in your business and trusts you to grow his investment. If the business is a partnership, the investor can be a full partner or a limited partner. If the business is an LLC, the investor can be an active member or silent member and his ownership stake is his percentage of membership shares. If it's an S-Corporation or C-Corporation, the ownership can be through common shares (voting, but near the bottom of the food chain for dividend or liquidation of assets) or preferred shares (nonvoting but near the top of the food chain for dividends or liquidation of assets) of stock in the company. Regardless of the type of business legal structure, you absolutely must formally clarify in writing exactly what this investor's role in the company will be. Because they are an actual owner in the company, not having a specific contract can cause a lot of problems later if the dynamics of the company change for the better or worse.

Venture Capital

Venture Capital (VC) is the Holy Grail of startups that need significant, up-front funding. And, like the Holy Grail, it is extremely difficult to obtain. VC firms invest in companies that convince them their investment would have a high probability of growing. If the business is successful, the VC prospers. VC firms are looking for the next Apple, Ford, Google, or McDonalds. But until they find it, they are looking for investments that will result in excellent profits.

VCs provide capital to young businesses in exchange for an ownership share of the business. VC firms usually don't want to participate in the start-up financing of a business unless the new company's management has a proven track record. Usually, they prefer to invest in companies that have received significant equity investments from the founders, which make the founders incentivized to ensure the company is successful. VCs also prefer to invest in companies that are already profitable, thus, reducing the risk.

VC firms prefer business proposals that have a competitive advantage or a strong value proposition in the form of a valuable patent, a high demand for the product, or a very unique (and legally protectable) aspect. The investment portfolios of most VC firms are stocked with high-risk investments that provide at least a 50% rate of return. The average return on their entire portfolio is usually at least 25-30% or more.

These investors rarely take a back seat with companies with which they choose to invest. They often take a hands-on approach and require certain representation on the board of directors and sometimes require involvement in the process of hiring key employees. The good news is that VC investors can provide valuable guidance and business advice. The bad news is that VC investors want substantial returns on their investments, and their need for high profits might be in conflict with those of the founders. It is interesting to note that many venture capitalists admit their portfolios follow the 2-6-2 rule. This means that in their experience, two investments will be wildly successful with high returns, six will yield moderate or break-even returns, and two will crash and burn.

Angel Investors

"If you don't have savings, and your cofounders are as poor as you are, and if Mom and Dad won't loan you money, then your best bet is to find people that know you— your friends. If they, too, won't help, then you're stuck seeking out angel investors." —Vivek Wadhwa[6]

Angel investors come in a variety of shapes and sizes. They're called angels because they are often initially viewed as a miracle to the recipients. They are usually found through personal or business contacts and many end up being family members, close friends, or someone your family or friends know. Angel investors are individuals and businesses that are interested in helping your business survive or grow. Their objective may be more than just focused on their own economic returns, but often profitability is a goal. They often have somewhat of a mission they follow, a reason they chose to help your business. That mission might be a personal relationship with a business owner, an interest in the demographic or geographic target that the business serves, or a desire for profitability. This mission might cause them to make specific demands on your business. Often times, angel investors focus on early-stage financing or last minute dire needs and the funding amounts they tend to provide are often smaller than what a venture capitalist might provide. However, having an angel investor on board will make your business more attractive to other potential investors.

Investment Banks and IPOs

The primary function of investment banking firms is to help businesses with a strong growth history and extremely strong growth potential *go public*. These firms help companies offer stock to the public through an initial public offering (IPO). Only C-Corporations can offer stock to the public. People or companies that own shares of stock in your corporation are partial owners of your company. If you have a truly hot business, this can be a good way to raise capital.

Entrepreneurs sometimes dream of IPOs, but this usually doesn't happen until a company has been in business for multiple years and has a proven track record of profitability, well-known management stability (e.g., the primary backer's name rhymes with "Gill Bates"), or there is strong demand for the company's products or services. To get to the point of being able to offer an IPO, the company usually has already gone through a few rounds of private funding.

Warrants

Warrants are a type of security used for long-term financing. They are a tool used by start-up companies to encourage investment by minimizing downside risk to the investor and providing significant upside potential. It grants the warrant owner the right to buy additional company stock at a predetermined price, called an *exercise price*, before a specified expiration date. The value of the warrant is the relationship of the stock's market price compared to the warrant price of the stock. If the market price is higher than the warrant price, the investor can enjoy the privilege of purchasing the stock at a discount. If the market price is lower than the warrant price at the time of expiration, the warrant is useless. Warrants are frequently attached to preferred stock or bonds or as a sweetener to encourage investing because they can often be detached from the stock or bond and sold separately.

Expand Your Team

Investors often just want to see the return on their investment. As mentioned in sections above, some investors want to get involved to ensure their investment risk is going to succeed, and the business owners need to weigh their need for funding against their willingness to share some aspect of control. Entrepreneurs who are aware of a talent deficit within their organization can sometimes capitalize on an opportunity to not only bring in necessary talent, but to bring in talent who has both investment dollars and a passion for your industry.

Finding these types of team members is not as simple as opening the yellow pages and looking up "Perfect Partner Investors," but usually they are closer than you might expect. The key is finding people with the talent you need and recruiting them. One technique might be to ask them to meet you for coffee so you can pick their brain. At the meeting, ask them a little about their background and try to get them talking about their experience and skill set so you can feel confident that they might be a good fit. At some point, you'll need to share your vision about your business and explain the talent deficit or the problem the deficit is causing. Ask them for advice and listen to it. Even if you do not feel they'll fit your need, they might have some valuable advice that only costs you a cup of coffee, which is much cheaper than hiring a consultant. If you think they would be a good fit, you need to eventually ask them if they would be interested in becoming an investing member of the team. You can also recruit your friends and family to help do the same thing and bring you potential leads.

Bootstrapping Techniques

"Sometimes your best investments are the ones you don't make."
—Donald Trump[7]

Bootstrapping a business is an effective and low-debt way to help ensure a positive cash flow for your business. It is an umbrella term that involves using any of a variety of techniques to help you use money wisely without over committing yourself to debt. If you must to resort to loans, be aware that it's easier to obtain loans for equipment, buildings, vehicles, and other assets, but it is harder to obtain loans to cover working capital for your raw materials or inventory. You'll need to keep as much cash on hand as possible through bootstrapping techniques.

Generally speaking, bootstrapping requires careful management of your financial resources. Be aware of your financial figures and work diligently to keep your overhead low. Every dollar of savings is a dollar of automatic profit. If you need to pay high prices for something, make certain you can justify the price, and that it will pay for itself when compared to a lower-priced or pre-owned equivalent. For example, brand new office furniture can cost many times as much as quality, pre-owned furniture. Do you really need an expensive, high-traffic location for a business that doesn't need to be in a high-traffic area?

Many billion-dollar entrepreneurs used bootstrapping to grow without external financing and to ensure the creditors wouldn't control their destiny or collect a large chunk of their profits. As you can see by the techniques listed below, there are numerous creative ways to limit debt and increase profits.

"I need to be in control of my own destiny."
—Richard Schulze, founder of Best Buy[8]

Bartering

Bartering is the exchange of goods or services without the use of money. Instead, the price is paid through the exchange of other goods or services. An advertising company can offer to provide free advertising to a computer repair technician in exchange for help setting up a wireless network in their office. The key is ensuring that whatever you are planning to trade in exchange for something else has equal value, or at least equal perceived value. It is also important to ensure that you really need what is being offered in the barter. If someone is offering to trade homemade candles for an automotive brake job and the owner of the auto repair business already has a house full of candles, this might not be worthy of a bartering trade.

If you have a product or service that has a high value to other business owners, but a rather low cost to you, you are in an excellent position to barter. Some of the best bartering potential comes from industries such as marketing, advertising, website development, printing, food industries, and consultants. Bartering is a nice tool to have, especially in tough times. It is also valuable for startups not only because they save money, but they provide experience and a customer base.

Don't be afraid to initiate the offer to barter for goods and services when appropriate. A café might offer twenty-five free lunches to a web designer in exchange for $250 worth of web development. From the café's perspective, twenty-five free lunches might cost them only $100 to provide, but it will help invoke a habit of frequenting their café and it might result in additional purchases later. Exchanging the lunches for $250 worth of web development is a great idea because they're getting it for only $100 of cost, not profit, if the web developer uses all twenty-five free lunches. From the perspective of the web developer, it might be a good deal because the website work might be fairly simple to complete using only an hour or two of time. Getting twenty-five free lunches they'd otherwise have to pay for seems like a great trade because they could take potential clients out to lunch for free, possibly get a great testimonial from the café client, and maybe even assign the project to a junior programmer who needs the experience.

Negotiating

In some cases, you can negotiate pricing. Ideally, a win-win situation is best so both sides of the negotiation feel good about the outcome. However, if you are bootstrapping your business, you need to protect your finances. It's okay to share that information with the person you are buying from or selling to. While the price tag on new items is often set firm in large stores, the price in independently owned stores is sometimes negotiable if you are dealing with the owner.

"*Everything is negotiable. Whether or not the negotiation is easy is another thing.*" —Carrie Fisher[9]

You can attempt to negotiate the price when buying anything from a private seller. There is no harm in offering less than the asking price. At the very least you can buy it for the asking price, if you really need it, but at the very best, you can purchase it for a significant discount. All you have to do is ask.

The same holds true for someone desiring products or services from you.

Be aware of some basic principles:

- The general goal of a successful negotiation is to find the lowest price for which the seller is willing to provide the product/service AND the highest price at which the purchaser is willing to pay in order to get the product/service.

- If a price is not settled on, the item/service will not be sold. Neither party wins.

- The more the buyer shows that he obviously wants something, the more he will be willing to pay for it. Someone overly excited about getting a specific item will have a tougher time negotiating the lowest price. Likewise, the more a seller wants to sell something, the more the buyer will be able to get the price lowered. A common strategy in negotiating is to appear very willing to walk away from the negotiation if a reasonable price isn't found.

- If one party buys or sells for a price they are not comfortable with, that party did not negotiate well and will have regrets later. If the purchaser has the regrets, they may not do business with that seller again. If a seller has regrets, they will likely overprice something to make up for it (e.g., warranty insurance).

- If either party was secretly willing to buy for a higher price or sell for a lower price, that party will feel like they got a good deal in the negotiation. A "win-win" situation occurs when both sides feel like they got the better deal.

- Win-win situations are actually better for you then being the only one who wins. One way to ensure a win-win is to find out what the deal-breaker price is for the other party, and then offer the other party a slightly better deal. This assumes that the price is well within your comfort level. This helps the other party feel like they got a good deal and be more willing to do give a little next time. For example, a buyer who felt like they got a good deal is likely to pay a slightly higher price for an additional item or add-on, and come back to business again in the future. A seller who feels like they got a good deal is more likely to throw in a little extra service (e.g., discounted shipping).

Below are some areas that are often overlooked as places where negotiating can save you money:

- By default, voucher deals such as Groupon and LivingSocial pay the merchant only half of the price for which you buy them. A $40 product or service might cost a voucher purchaser only $20 but the merchant only gets $10. This means the merchant is providing a $40 product or service for $10, which isn't normally a good business deal. Knowing this, you might be able to approach the merchant directly and offer them $15 for that same product or service, which would give them an extra $5 of revenue for the discounted item. As long as the merchant hasn't negotiated a better deal with the voucher provider so they get better than the default, this would, financially, be a good choice for them.

- Returned items, discontinued items, and last-on-shelf items. Even when purchasing from a major retailer, these items are usually marked down in order to sell. Most department managers have the ability to mark them down an additional amount, especially if you have to "settle" for that item because you can't find it new.

- Used item resellers such as used vehicles, used furniture, equipment, and more, often have a lot of price flexibility. Sometimes the flexibility comes from the seller's commission on the sale, and sometimes from the base price itself.

- Estate sales, business asset liquidation sales, and large garage sales can be surprisingly valuable sources of items for your business. Furniture, decorations, artwork, tools, equipment, kitchenware, office supplies, computers and printers, networking equipment, and more can be found at these types of sales. The best part is that everything is negotiable. Think about win-win. The main goal for estate and liquidation sellers is to get rid of everything while still getting the most money in the process. However, getting rid of everything is essential. Buying one item doesn't get you a lot of negotiating room unless it's an item that few will want. Being willing to buy a whole set or combine several items gives you a lot more negotiating room.

- The terms for leases and rentals are almost always negotiable and can save significant money.

Lease Financing Companies

Companies that will lease you equipment, vehicles, software, buildings, services, and systems are often a good way to save money up front without paying an initial outlay of cash for the asset. Most leases are a form of renting the item for a specified period of time. You might, for example, lease a building for five years, a car for two years, a copy machine for one year, or a software package on a month-to-month basis. Many times the lease agreement will be between your company and a lease finance company, not necessarily the company who is providing you with the asset.

Think about it this way: if you decide to buy a small commercial building for $500,000 to operate your start-up business in, it will require a significant amount of funding up front and will tie up a large amount of your assets due to the purchase or financing. However, getting into a lease for $3,000 per month will likely be a lot easier to accomplish and can save your assets for other business startup needs. There are other advantages to leasing something as expensive as a building. If your business outgrows the building or you want to move to a larger or smaller facility, you'll be glad you decided on a lease, as you won't have to figure out what to do with your asset.

Using software as a smaller-scale example, you might be able to purchase a software system for $1,000 or lease it for $50 a month. Being able to save $950 up front is a nice advantage for a cash-strapped business, but over time the business will end up paying more for the software than if it had just bit the bullet and paid the full price up front. But in the process of bootstrapping and trying to avoid debt, leasing might make more sense.

The downside of leasing is that you don't actually own the item; therefore, you are basically providing wealth to the owner, and at the end of the lease term you return the asset, renew the contract for a longer term, or buy the used asset. Because the item is being borrowed, if you fail to make payments, the leasing company will take back their item. If you lease something long term, your payments might be low, but in the long run, you could have purchased a new item for less money, sometimes several times over.

The upside of leasing is that you don't actually own the item. Yep, it's both good and bad, depending on your situation. Your credit isn't as much of a factor when leasing an item as with financing the purchase of an item. Also, many lease contracts include free or discounted repair or replacement in case the item has a problem, thus taking that risk off your business. Because it's only a temporary ownership, you're not stuck with an item that might become outdated. If a better model comes along, you can often upgrade it, which is unlike purchasing an item with which you are stuck. Also, if your business fails or has severe financial problems, it's easier to get out of a lease contract than a purchase. Some people like leasing cars so they can continually drive the newest models. Copy machines are often leased so businesses can avoid the expensive purchase of a new one, and they can get free repairs since copy machines can be expensive to fix.

WARNING

Shop around and know the differences before you commit. Leases often require a down payment. Be careful that you don't put so much money down that you end up spending the same, or more, for the asset than if you had just bought it with a down payment and made payments. Remember the reasons why you want to lease this item, then make sure it pencils out to meet your goal.

Financing Companies

Instead of paying full price for assets up front, which requires dipping into precious start-up cash reserves, you can often finance your purchase. Breaking down big price tags into monthly payments is a nice option that allows companies the ability to buy equipment, supplies, and inventory on credit. Financing companies charge an interest rate that is built into the payments. This interest helps them not only profit from loaning you the money, but also cover some of the collective risk they incur because of bad loans that don't get fully paid off.

A finance company is often the company from which you make the asset purchase. For example, the furniture company might provide financing for purchases and, sometimes, even give you a free six months up front before the first payment is due. Don't be afraid to shop around for good deals. Do the calculations to figure out what you'll be paying for the item when you finally finish paying it off.

BIZ TIPS

Do the math! It is important that you take a moment to calculate what an item is really going to cost you after you pay off the interest that will be applied when you finance the purchase of the item. Financing processes often deal with an APR (Annual Percentage Rate). It's easy to figure out if you know a few details about the loan and can do some simple algebra.
Let's say that you want to buy an item for $1,000 and the APR is 10%.

The first thing you need to find out is whether the APR is calculated yearly, monthly, or daily. If they are calculating interest on a yearly basis, you'll pay a flat 10%, or $100 every year. If you are paying interest on a monthly basis, you'll divide the 10% by 12 annual payments. Thus, 10% ÷ 12 = 0.83%, which is $8.30 per month. If you are paying interest on a daily basis, you'll divide the 10% by 365 annual payments, which amounts to 10% ÷ 365 = 0.02%, $0.20 per day.

The next thing you need to find out is which of the three types of APR it is—fixed, variable, or tiered. Fixed APRs remain constant for the life of the loan. Variable APRs can fluctuate daily, thus making it a guessing game as to how much interest you are really paying. Tiered APRs have interest rates that change at set periods of time so the interest rate depends on which tier is active.
It's also important to know whether the APR is front-loaded or rear-loaded. If it's in the rears, you pay interest for the time period that just passed. This can help you decide when to pay it off. That's why it's wise to pay off a credit card bill before the month passes because the interest gets tacked on at the end of the month so if you pay it off before that point, you basically got to borrow the money for free.

For more details and some helpful, online financial calculators (interest, mortgage, and other loans), scan this barcode or go to www.HireSelf.com/business-financing

www.HireSelf.com/
business-financing

Prepaid Customers and Advanced Sales

Many start-up business situations allow for prepaid products and services. Website developers can collect half of the payment up front. Manufacturers can take payment before creating the product. These advanced funds can be used to purchase equipment or inventory necessary to provide the service or product. You might need to offer a discount for up-front payment, but because you are still in start-up mode, you need to make sure you can deliver. Your reputation can propel future business.

There are a surprisingly large number of entrepreneurs who started, or significantly advanced, their business through payment advances by their customers. The following are real-life examples example:

- Josh Isaak, the cofounder of ClinicRise in the US, made $16,000 in presales before the product was even built.[10]
- DreamQii, a robotics company, set a fundraising goal of $100,000 for PlexiDrone, aerial photography. They exceeded their goal by ten times that amount—$1,009,041.[11]
- Pebble Technology raised $10,266,845 for a smartwatch that synched to a smartphone.[12] They presold thousands of them when they had nothing more than a prototype at the time.
- The book you are reading raised $3,737 for publishing costs and presold over one hundred copies before a single chapter was completed.

Trade Credit (Buying on Credit)

Vendors and suppliers will often sell to you on trade credit. Ask around because not everyone offers this feature, and if you make purchases carefully, you can save money by avoiding debt. Under normal circumstances, this type of credit is usually only offered to regular customers because suppliers want new, unproven clients to pay ahead of time or cash or check on delivery (COD) until you've proven yourself as reliable. However, if you purchase from a trade show, you can often get "show specials" that offer even better incentives from the supplier. Often, you have to fill out a credit application for them, but the actual credit requirements are sometimes minimal. Sometimes you can negotiate a trade credit with suppliers, especially small suppliers where you are able to talk with the owner, especially if they think they will be your ongoing supplier. Sometimes, having a good business plan can convince some to help you out.

This can be a good source of short-term financing for both start-up companies and growing businesses because, depending on the deal they give you, you can often delay payment for 30, 60, 90 days or even longer without paying interest. These specials can also include free shipping and financing, so you can pay off the bill over time as your sales grow. If you are buying items to resell or combine into a product for sale, this can be extremely valuable if you are able to sell enough of the product to cover the upcoming payment.

Be smart when using trade credit. Sometimes, using it on a continual basis is not a good long-term solution. Your business may become too committed to those suppliers without allowing yourself to remain flexible and continually shop around for more competitive suppliers who might offer lower prices, a superior product, a better return policy, more reliable deliveries, or better support. Sometimes buying only for the benefit of trade credit can end up costing you more in the long run as your business grows, if you do not allow yourself the flexibility to compare them against their competition.

Letter of Credit

In special circumstances, you can use a letter of credit from a customer who has pledged to pay that might convince a supplier to provide you with trade credit. This can be a nifty way to avoid going into debt during the time you buy from a supplier and receive payment from the customer.

For example, let's say that your business sells handmade hairpieces that require exotic feathers that you obtain from a supplier. A customer places an order for a large quantity of your hairpieces and is willing to write a letter of credit to you as proof that they will pay for those hairpieces when they are ready in thirty days. Your business can then use that letter to convince your feather supplier to provide you with trade credit to cover the time needed for you to build the hairpieces and receive payment from the customer.

Factoring

Factoring is a way to quickly liquidate your receivables (money owed to you by your customers) by selling those receivables to a buyer, also called a factor, such as a commercial finance company. This is usually only done in industries where long receivables are part of the normal business cycle. Factors usually buy accounts receivable at a rate ranging between 75 and 90 percent of the face value and add a discount rate of between 2 and 6 percent. The factor assumes the risk and task of collecting the receivables. As long as your profits are high enough to allow for factoring, you can still make money.

Sponsorships

Sponsors are individuals or corporations that provide financial or alternate forms of support to others in exchange for public recognition. Many larger companies look to increase their name recognition in exchange for offering money, products, or supplies. American Express acts as a sponsor and will happily provide free guest checkbooks, business card holders, menu covers, door stickers, hours-of-operation signage, and much more, if you will accept their credit cards through your credit card processor.

Apple and Microsoft are known for sponsoring school programs or business incubators with free or heavily discounted equipment or software in exchange for public recognition. Another aspect to this sponsorship is that the audience using their products is learning to use the products and forming skills and habits that will make them less likely to switch to something different when they move on. By taking the opportunity to provide products to a targeted audience, they invest in future sales and market share.

Tool companies frequently act as sponsors for auto repair companies, construction businesses, and racecar drivers. They provide money, tools, uniforms, and more in exchange for the display of their logo or an exclusive agreement to use only their tools during a set amount of time.

Companies with a track record of success or who are able to demonstrate they have a high potential for success are sometimes able to get sponsorships for various aspects of their business. By wearing or displaying their logo, posting a logo or link to the sponsor on their website, applying a sticker to their vehicle, or otherwise promoting the sponsor, a business can receive money, goods, or services in exchange as a nice way to help bootstrap their business.

AUTHOR SIDEBAR

When setting up our family restaurant, I did some research in trying to decide between Coke and Pepsi as my soft drink provider. After discovering that all of the surrounding restaurants carried only Coke products, I approached Pepsi and explained that I'm thinking about carrying Pepsi because no one else did in the surrounding area. They did some checking and called me back. I ended up getting a sweet deal because of the lucky situation I was in. Not only did I get a free eight-spout dispensing machine, free racks, pumps, and installation for my Pepsi equipment (which is fairly common), but I also received over a thousand dollars of free product, including eight bag-in-the-boxes (syrup), carbon dioxide tanks, cups, lids, a clock, and several advertising materials. I didn't use some of this, and I turned down multiple large cooling units because I didn't have the space to hold them, but my offer to bring Pepsi into the area saved me a lot of money because of the sponsorship. By the way, does anyone want a Pepsi clock?

Internal Revenue Service

No, the IRS is not into loaning, granting, or investing money in business start-ups, but it does allow you to deduct expenses for the profits you invest back into your growing business. Start-up companies are great sources of tax deductions, and depreciating equipment and building costs can be a nice financial gift of sorts down the road when your profits increase. Ensure you have a good relationship with your tax professional, and be strategic about how to prepare yourself to properly record and take advantage of those nice deductions.

Fundraising

It is amazing how many businesses use fundraising to produce income. Nonprofits are especially known for their fundraising skills. Most churches and many charity-type organizations sometimes survive entirely on fundraising and the donations of others. If your business is a nonprofit business, this might be an important aspect of your revenue stream. If you are registered with the IRS as a charity organization and take tax-deductible donations, you have an edge. From a tax perspective, donors would much rather give a tax-deductible donation instead of a non-tax-deductible donation.

Fundraising is the process of soliciting and gathering voluntary contributions of resources such as money, buildings, vehicles, equipment, supplies, stocks, trust funds, a financial endowment, or labor. When products or professional services are donated to an organization, sometimes for the exchange of promotion, the donation is called an in-kind gift.

Many companies rely on the proceeds from an endowment that has been setup after an initial sizeable gift, often from a will or major donor. Endowments can also be created and grown over time by saving up contributions until the endowment is large enough to fund its purpose. The endowment essentially provides the recipient organization with the annual interest from the initial investment. The enormous endowment created by Alfred Nobel funds the Nobel Prize program. Another endowment example, Fonds de l'entraide de la péninsule acadienne, was established with the objective to offer financial support for medical care to people in the Acadian Peninsula.[13]

Fundraising efforts are not limited to nonprofit organizations. Many for-profit companies embark on fundraising campaigns for various purposes, requiring the identification and solicitation of contributors.

Special events are another method of fundraising. These range from the traditional bake sale to formal dinners, special speaker events, concerts, raffles, and walkathons. These methods also increase name recognition for the business, and if the fundraising is for a for-profit business, sometimes a portion of the proceeds will be donated to a charity to encourage giving.

Selling a special product can be a form of product fundraising. The famous Girl Scout Cookies are a great example of this type of fundraising.

Many large fundraising efforts provide a legacy reward to the contributor. Legacy rewards include everything from plaques and certificates, to major contributor walls, and engraved bricks on sidewalks. Chairs, rooms, wings, and whole buildings are sometimes named after major contributors.

Charity ad books, programs, brochures, and signage are forms of donation in exchange for recognition. Your business can provide sponsorship opportunities, or display ads, signs, or promotional memorabilia at an event.

Corporations are giving billions of dollars every year as part of charitable giving programs, and well over half of the Fortune 500 companies provide an employee matching gift program to encourage their employees to give as well. Being able to tap into these programs can be huge for many companies, especially nonprofits.

Buy Used

What do you call a brand new piece of furniture or equipment that has just been put to use in your business? *Used* furniture or equipment! That brand new car becomes a *used* car as soon as you drive it off the dealer's lot. Buying used is a smart bootstrapping technique that can save significant money.

Consider this example: A brand new office desk costs $1,000. As soon as it becomes a used office desk, it is suddenly only worth $300, meaning that if you tried to sell it, you could only sell it for about $300. That's a whopping loss of $700 just to smell that fresh oak scent for a few days. Now let's say that you buy that same desk as a used desk instead of a new desk. You buy it for $300. If you had to turn around and sell it, guess how much you could sell it for? About $300! Buying many things used not only saves money on the front end, but those items retain most of their value if you turn around and sell them.

Certain types of equipment are best purchased new, but for the most situations, used equipment, furniture, and supplies will save you a significant amount of money. Buying new is a luxury, and people who are bootstrapping their business need to maintain discipline. Garage sales, craigslist, going-out-of-business sales, and the For Sale sections of your newspaper are valuable places to find business items for pennies on the dollar.

Affiliate Advertising

Many companies have found great ways to leverage their own websites, brochures, and marketing with affiliate advertising, thus producing residual income. This essentially involves selling advertising space to companies who can benefit from your target customers. There are excellent online affiliate marketing programs that can provide you with residual income through clicks, impressions, or purchases.

AUTHOR SIDEBAR

My software company created a virtual, online shopping mall back in 2000. We designed it as an experiment to test the idea of creating an entire website out of a database, and we had the wild idea of handpicking big-name stores that just happened to provide affiliate paybacks to us. The virtual mall and affiliate links were just a creative way to test the database technology. It worked great, but when we started getting a few paychecks from the stores we listed on the website, we started looking more closely at the affiliate business. We started to play around with algorithms to beat our competitors in search engine ranking for phrases such as "online clothing stores" and "discount book stores." We found some techniques that ended up ranking us #1 in almost every shopping category we targeted and at least in the top five. For around two years, we made around $500/month in affiliate marketing revenue for a website that we were only using to test a concept. Over time, Google kept changing the ranking algorithm, and we didn't have the time to continually tune the website to dominate rankings for desired searches. Our affiliate revenue started dropping as our client load started growing, so we let the website go dormant in order to focus on our clients. This experience made me a big believer in the power of affiliate marketing and its ability to produce residual and passive income.

Let's say, for example, that ProFlowers.com, a leading online source for purchasing flowers that will arrive fresh and in the mail of your intended recipient, is offering an affiliate program through a major affiliate business. They might offer you three different ways to get paid, or combine all three (these are fictional payoffs):

1. Impressions: They might pay you $1.00 for every 1,000 views of the affiliate advertising graphic. If you have a high-traffic website, and you see a million people a month, this can be a nice little chunk of

passive revenue sent to you just because you posted this ad through an affiliate program. The affiliate vendor is going after name recognition with your viewers and is hoping some will click on the link as well.

2. Clicks: They might pay you fifty cents every time someone clicks on the link from your website, whether or not they buy anything. In reality, this may range from a few pennies per click or it might be a few dollars, depending on whether your target audience is their target audience. Your ability to recommend the company or its product might help encourage someone to click on it, but you want to make sure you maintain credibility by not recommending junk, or your viewer won't trust you next time.

3. Purchases: ProFlowers might give you 30% of a purchase transaction that results from your efforts to send customers their way. This doesn't cost the customer anything extra; the retailer is paying you the finder's fee out of their own revenue. In reality, and depending on the affiliate partner, this can be a fraction of a percent, or up to over a whopping 70%!

As you can see, affiliate marketing can be a great source of residual income to help you build up revenue while you sleep.

SOURCES

If you'd like to read some additional techniques for obtaining residual income through affiliate programs or see a list of excellent affiliate marketing programs that offer links and ads for your website, newsletter, or blog at no cost to you, scan this barcode or go to www.HireSelf.com/affiliate-marketing

www.HireSelf.com/
affiliate-marketing

Crowdfunding

Crowdfunding, also known as crowd financing, is a process in which businesses or individuals commit money or other resources to fund projects initiated by other people or organizations. This usually involves large numbers of small contributors, but the results can be enormous.

Crowdfunding usually takes place through an online portal that handles the legal contracts, as well as the pledges and financial transactions involved. These online portals also provide features to promote the project, usually with in-depth descriptions, images, and video. Most also provide social networking and a reward or incentive system for backers.

Crowdfunding is relatively new and is quickly gaining popularity. Federal and state governments are moving to enable some reasonable structure around crowdfunding possibilities. Because the laws are changing so quickly, you will need to read up on recent changes in your state and country.

There are literally dozens of crowdfunding services in existence and the list is growing. There are two main categories that could apply to business ventures, and each category has different types of investment models.

The first type of crowdfunding service supports raising money for products, goods, or service ventures. There are three standard models of how funds are handled, and some crowdfunding services allow you to select between them:

1. All or Nothing: The project owner sets a minimum amount of needed funds to complete the project, and if that amount isn't pledged by backers, no one has to pay anything, and the project owner gets nothing. If at least the minimum amount is pledged, the crowdfunding service will collect the pledges, keep a percentage for providing the service, and pay the project owner the balance.

2. Keep Everything: The project owner keeps everything that is pledged, minus a fee kept by the crowdfunding service. If the owner doesn't raise enough funds to complete the project, it is up to them to find other financial sources to complete it, or refund the contributions.

3. Bounty or Kitty: The funds are raised to solve a specific problem, and whoever is able to do so, gets to collect the bounty. For example, if someone creates a project to raise money to fix a software bug, others who want the same solution can contribute to the bounty to

reward the solution provider who gets approved by the contributors before collecting the bounty.

The two largest crowdfunding sites in this category are Kickstarter and Indiegogo. Kickstarter is an all-or-nothing model, and Indiegogo allows the project owner to decide whether the project is all-or-nothing or keep everything.

Kickstarter facts:

- Kickstarter officially launched on April 28, 2009. Since then, well over $1,000,000,000 (yep, that's one *billion*) has been pledged to fund projects by 5.7 million people. Over 17,000 individuals have backed more than fifty projects each.
- Funded projects include restaurants, satellites, inventions, books, movies, food trucks, plays, art projects, video games, board games, and even the book you are currently reading or listening to!

The second type of crowdfunding supports business ventures. It can be used to raise capital (equity) or to borrow money on specific terms. There are three primary types of business venture crowdfunding services, but there are numerous others that are tuned to very specific needs or services:

1. Equity Funding: Investors receive equity in the company that is raising funds.
2. Property Funding: Investors receive some form of interest or ownership of the property from the project owner raising funds.
3. Debt Funding: The project owner borrows money and must repay it, usually with interest.

At the time of writing this book, one of the biggest business venture crowdfunding sites in this category is MicroVentures. We originally listed another top company, ProFounder, but then discovered they closed their doors. Follow the link below to get an updated list of crowdfunding companies.

AUTHOR SIDEBAR

Because I knew I wanted to include a section on crowdfunding, I thought it would be wise to experience it myself so I can speak authoritatively about it. I had backed a few crowdfunding projects in the past but had never attempted to post a project myself. I decided to make a project for this book to help cover the costs of cover design, formatting, and printing. It was a lot of hard work, but it paid off. We used Kickstarter, the biggest crowdfunding site on the planet, and raised $3,737 which exceeded our all-or-nothing goal of $3,500. Before launching the project, I spent a month reading numerous books and articles on the subject, and studying several hundred projects to figure out why they succeeded or failed. I interviewed dozens of highly successful project owners to find out what made the difference. I then wrote some detailed marketing information, created a video, developed some very creative rewards (one of which provided a cool team of secondary editors who paid to edit this book), and presold over one hundred books in the process! If you want to read more and learn some valuable information I learned along the way, see the Sources sidebar below for the website link.

SOURCES

For more information about how this book used crowdfunding, as well as a helpful list of crowdfunding websites, scan this barcode or go to www.HireSelf.com/crowdfunding

www.HireSelf.com/
crowdfunding

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