

Financing Information

When starting a business, one important consideration is where to obtain capital to bank your venture. Most start-up businesses require a capital contribution by the entrepreneur, usually 20%. The remaining financing may be available from local banks or may require private investors. There are several Small Business Administration loan programs available to businesses, all of which require bank participation. These loan programs, however, are not guaranteed. They are all subject to change based on the SBA's current budget.

- **SBA Basic 7(a) Loan Guaranty.** This program serves as the SBA's primary business loan program to help qualified small businesses obtain financing when they might not be eligible for business loans through normal lending channels. Loan proceeds can be used for most sound business purposes including working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements, and debt refinancing (under special conditions). Loan maturity is up to 10 years for working capital and generally up to 25 years for fixed assets. The maximum SBA will guarantee is \$2,000,000 and not more than 75% of the total loan.

- **SBA Certified Development Company (CDC), a 504 Loan Program.** This program provides long-term, fixed-rate financing to small businesses to acquire real estate or machinery or equipment for expansion or modernization. Typically a 504 project includes a loan secured from a private-sector lender with a senior lien, a loan secured from a CDC (funded by a 100 percent SBA-guaranteed debenture) with a junior lien covering up to 40 percent of the total cost, and a contribution of at least 10 percent equity from the borrower. In other words, the SBA takes a second lien position behind the bank. The maximum SBA will guarantee is \$1,500,000. Job creation is a requirement of the program.

- **SBA Microloan, a 7(m) Loan Program.** This program provides short-term loans of up to \$35,000 to small businesses and not-for-profit child-care centers for working capital or the purchase of inventory, supplies, furniture, fixtures, machinery and/or equipment. Proceeds cannot be used to pay existing debts or to purchase real estate. The SBA makes or guarantees a loan to an intermediary, who in turn, makes the microloan to the applicant. These organizations also provide management and technical assistance. The loans are not guaranteed by the SBA. The microloan program is available in selected locations in most states.

While each of these programs has specific requirements for eligibility, there are certain standards that must be met for all loan programs. A loan applicant must be of good character; show the ability to operate a small business successfully, and have a reasonable amount of his/her own resources to invest to withstand possible losses. In addition, the following will likely be required:

- Credit Report
- Collateral adequate to secure the debt. List of collateral and its value
- Appraisals required on real property used as collateral
- Personal guarantees required of those persons (or companies with 20% ownership)
- Secondary collateral may be required
- Personal financial statements & financial statements of business (if applicable)

**Amounts and conditions for all Small Business Administration loans are subject to change.
www.sba.gov*

How to Apply for a Loan

You must first seek financing from a bank or other private source. If that is available at reasonable terms, the SBA cannot make a loan. Take your business plan to your banker and discuss your financial requirements with him/her. His/her involvement is essential. Then, call the Small Business Development Center at 706-272-2700 to discuss the project's eligibility for SBA assistance.

Steps to Make Your Loan Proposal Stronger!

In today's financial environment, banks have plenty of cash to lend but find themselves in a regulatory squeeze requiring that they issue loans only to the best applicants. "Best" is defined as being closest to zero risk. Gone are the days of the "character" loan to help you get over a crunch or a "confidence" loan to fuel projected growth. A business start-up loan you ask? You better rely on persistence. If you are going to obtain a business loan, you need now more than ever to do your homework. Do not try to take shortcuts with your friendly loan officer. Cover all the bases your first time out!

This is a quick list of seven common errors or omissions found in failed loan requests.

- 1.** Many applicants have not **prepared the required documentation** to support the loan proposal. The most common is the omission of a sound business or strategic plan. Not every business loan requires a business plan, especially if the business has a history of a strong cash flow. However, most banks require existing businesses to produce two or three years of financial projections along with a description of the project and history of the business. A new business will need a full business plan to explain the cash requirements and management issues of the business. For existing and new businesses, if a loan officer asks to see a three-year plan and it is not available, management looks bad.
- 2.** Many small business owners actually go to a bank not **knowing how much money they need** to borrow. Nothing is more frustrating to a lender when he or she hears, "Well, how much can I get?" Always be specific about the loan amount and provide a detailed schedule showing how you intend to use the borrowed money and clearly demonstrate the need. Do not borrow more than you need.
- 3.** If you do not **document how you intend to pay the loan back**, the deal is dead. Ordinarily, business loans must be paid back through continuing cash flow. To demonstrate repayment, three years of Historical Statement (Balance Sheet and Profit & Loss) are mandatory. Cash flow projections showing the impact of the loan for the first 12 months are a must. Make sure your financials are credible. Poorly prepared statements, especially internally prepared statements, are the kiss of death.
- 4.** Many applicants are not realistic about **how much and what type of asset-based collateral is needed** to put their request over the top. Don't expect to obtain a long-term loan (five years +) secured by inventories or receivable (current assets). You must be prepared to reach into your personal net worth and put up the hard stuff, mostly real estate. If you show reluctance to offer what you have, "doubt" about your confidence and commitment to the enterprise creeps into the application and the process gets tougher. Don't overstate the quick sale value of collateral; be realistic. Eventually, you will have to get appraisals, and if they come in short, you will have wasted everybody's time.



Steps to Make Your Loan Proposal Stronger! (Continued)

5. Aggressive tax strategies that result in no year-end tax obligations because no profit is claimed by the firm will result in no **evidence of repayment ability** in your application. Federal tax returns, both personal and business are the final determinant of company performance and management integrity. Always claim 100 percent of your income, and whatever you do, don't plead to your banker, "It's done all of the time." You've just revealed that there is a huge contingent tax liability looming out there that could result in the business being closed when you're sent "up the river."

6. You should not ask the bank to do it all. Some applicants neglect the net worth component of the balance sheet. If the loan request puts the bank in over four times your net worth, the application is on shaky ground. High debt compared to your stake in the business gives the bank excessive control over the operation, and they don't want to own your company anyway. Keep things reasonable in owner's draw or officer's salary. Don't raise the possibility that the company is being milked. Before you submit your loan application, go to the library or go to your local SBDC and find the latest edition on the Robert Morris and Associates' (RMA) Annual Statement Studies. The Statement Studies contain composite balance sheets and income statements for more than 360 industries. This is valuable information for comparing your company to the industry, and more than likely your banker will evaluate your business based on this book or another similar source such as Dun and Bradstreet.

7. Don't be reluctant to tap into the vast amount of help to **get a first class loan proposal** pulled together. A good loan package or accountant will charge for this service, but it will be money well spent if you're not sure you can tackle the job yourself.

This statement is especially true if government programs are involved, i.e. the U.S. Small Business Administration. Preparing and submitting a business loan proposal can be a complex process, but with a common sense attitude and help from the Small Business Development Center, it will be a fruitful experience. Banks are in the business of lending money; keep that in mind. If you get turned down, keep trying. Your project may be the perfect loan for a banker down the street.

Tony O'Reilly, Executive Director of the Small Business Assistance Corporation in Savannah GA.

EXERCISE FOUR: How Much Cash Will You Need to Start?

Use this worksheet to help determine how much money you'll need to start your business

Estimated Annual Sales _____

(This is the YEAR ONE goal you have set for yourself. Use this number as a basis for estimating the amount you'll need to spend each month, in order to meet this goal.)

Estimated Monthly Expenses

- _____ Salary of Owner/Manager (how much will YOU make each month?)
- _____ All other salaries/wages (will you have additional staff?)
- _____ Rent (building and equipment)
- _____ Advertising per month
- _____ Monthly Office Expenses (supplies, etc.)
- _____ Telephone and Fax
- _____ Computers and Internet Service
- _____ Utilities
- _____ Insurance
- _____ Taxes, inc. Soc. Security
- _____ Maintenance/Repairs
- _____ Monthly Legal/Professional Fees
- _____ Loan Payments
- _____ Miscellaneous

1. _____ SUBTOTAL of Monthly Expenses (add all expense lines, above)

2. _____ (Multiply SUBTOTAL 1 by the Number of Months in which you do not anticipate having enough income to fully cover your expenses for a month. If you estimate that to be three months, multiply the amount in line 1/SUBTOTAL above, by 3. If you estimate it to be six months, multiply the amount in line 1 by 6. Remember to allow time for building a customer base, performing the services or selling the product, and more time, for collecting payment from clients.)

One Time Start Up Costs

To determine these amounts, get specific estimates from suppliers, contractors, professionals and/or government authorities to ensure accurate amounts.

- _____ Fixtures & Equipment
- _____ Decorating & Remodeling
- _____ Installation of Fixtures/Equipment.
- _____ Starting Inventory
- _____ Deposits for Utilities
- _____ Startup Legal/Professional Fees
- _____ Business Licenses & Permits
- _____ Advertising & Promotion for Opening
- _____ Other

3. _____ SUBTOTAL of Startup Costs

4. _____ TOTAL ESTIMATE OF CASH NEEDED
FOR START UP (Add Lines 2 and 3 to get this number)

LINE 4 equals the amount of cash you need on hand, to start your business and be successful. If you don't have easy access to this amount of cash flow, you need to consider a small business loan or other funding. Contact the Greater Rome Chamber of Commerce for a list of financial resources, or visit the Chamber website at www.romea.com.

