Small Business Financing

We **do not** endorse or recommend any products, services, or organizations.
Please undertake due diligence before buying or using any product or service.

1. To understand some financing basics, let us start with a few points:
   a. Profits are important (i.e., revenue of the business minus costs). This is the business's income. To acquire financing for your business, in most cases, it needs to have income substantially higher than its debt payments.
   b. Equity is important. Equity, in short, means the amount of money you invest in your business. Your business equity is similar to your personal Net Worth. On your Business Balance Sheet, your Assets should be higher than your Debts. Without positive equity, the business is more at risk for defaulting on its obligations. More equity relates to less risk for the lender.
   c. Positive cash flow is necessary to pay debts. Some lenders might require cash flow projections showing double the cash needed to pay debts after all expenses.
   d. Why are the above important? Because a lender will evaluate your business for risk. Lenders are risk-averse. In other words, the lender wants some assurance the loan will be paid back.
2. Use an accrual accounting system instead of a cash system. Accrual is slightly more complicated but shows accounts receivable, payables, and inventory changes. If you have any of these, the numbers are needed to evaluate the business's financial position.

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3. The business might not have a credit score, but the owner or buyer should. Review your credit score for free at annualcreditreport.com. The score typically required to qualify for most loans is about 600 or above. Expect the lender to require a personal guarantee. A personal guarantee means you will be personally responsible for paying if the business cannot pay. Understand all of your financial and legal obligations related to small business financing.
4. Pay all your bills on time, every time (if possible). It will likely improve your credit score.
5. For most newer small businesses (i.e., in business less than three years), it will be challenging to obtain business credit unless the business has substantial security or a record of substantial bank deposits to offer as collateral. To clarify, collateral is something that can be offered to satisfy a loan if it cannot be paid.
6. Banks usually want to review tax returns and financial statements to assess strengths and weaknesses. This is a common practice.
7. Commercial bank loans are rare for small start-ups (i.e., again, in business less than three years). Start-ups do not have enough of a track record for banks to evaluate the risk. More risk results in higher loan costs or denial of a loan. Alternative or online lenders can be exceedingly expensive. Business borrowers do not have consumer loan protections. Check the fine print and an annual percentage rate ("APR") that includes fees.
8. Before pursuing financing of any type, undertake due diligence, and discuss with a Certified Public Accountant, lawyer, SBDC Consultant, and other professionals. Contact our office today as we can help: idahosbdc.org.

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