



THE OHIO STATE UNIVERSITY

COLLEGE OF FOOD, AGRICULTURAL,
AND ENVIRONMENTAL SCIENCES

Business Financing 101

What It Takes to Borrow Money





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Financing is ...

- A means to accomplish short and long term goals for the business.
- A strategic tool to facilitate taking a calculated risk to obtain a future reward.
- For most, a necessary part of doing business today.



Financing includes ...

- Real Estate Loans, construction loans, credit lines, term loans & leases obtained from a traditional lender
- Overdraft protection on checking accounts
- Credit cards
- Trade accounts with suppliers
- Non-traditional sources, such as private individuals



A Good Banker/Lender is...

- A trusted advisor who is willing to LISTEN to your dreams and goals, and is not just out to sell a product.
- Has your best interests at heart for the long-term, even when the answer is something you may not want to hear.
- Can customize solutions to fit your needs (within prudent lending standards).
- Willing to help clients understand what they need to do to “get to the next level.”



A Good Customer ...

- Is honest with their banker and keeps him/her informed, especially when facing financial challenges.
- Provides complete and accurate information as needed on a timely basis.
- Recognizes the importance of maintaining good credit history & pays bills on time.
- Understands that the relationship must be mutually beneficial for both parties.
- Realizes their banker is not their enemy!



5 Basic Components of Credit Analysis

- Capital
- Conditions
- Character
- Collateral
- Capacity





Capital

- Applicant's equity or net worth
- Owner's personal investment in company
- How much risk are you taking
- Can provide a "Plan B" repayment source
- Type of business – differences in needs





Conditions

- Local economic climate
- Other industries could affect your business
- What is the purpose of the loan
- Political influences/ history
- Competition





Character

- Check on your company's financial status
- Personal credit history/creatures of habit
- Experience
- Responsible company leadership
- Timeliness in fulfilling obligations





Collateral

- “Plan C” Repayment Source
- Anything of use for security of repayment
- Personal Guarantees
- Hard Assets, Accounts Receivables, Inventory, Goodwill
- Loan to Value Ratios





Collateral Discounts or LTV's



- “Are based upon perishability and/or liquidation value
- Allow “cushion” for potential fluctuations in value.
- Prior liens are subtracted after discounting to find net available value.

Typical discounted values for businesses -

- Inventory—40-50%
- Equipment—50-75% (age, condition, market?)
- Real Estate—75%
- Some inventory & equipment may have little or no value because of limited resale market



Capacity

- Repayment ability
- Ability to get repaid
- Cash Flow !
- Innovation, education, knowledge, experience
- Consideration of other liabilities





Common Sense

- What is the specific purpose?
- What amount do I need--not how much can I (or want) to borrow? *(Itemized listing of use of funds)*
- What collateral is available?
- How much cash can I put in the deal?
- Terms: What rate? How long? What is the estimated payment?
- Can I repay the loan?





Credit Check

- Hard inquiries
- Available balances on open accounts
- Payment history
- “Maxed Out” credit lines
- Debt to income





Consumer Credit

- Credit history
- Employment history/ earnings potential
- Stability (residency, personal reserves etc.)





Commercial Credit

- Commercial number years in business
- Type of business (retail, service, manufacturing etc.)
- Legal structure
- Location
- Seasonal vs. non-seasonal
- Area market, industry in general
- Management strength





Things that make your lender happy ...

- A down payment!
 - 20-25% is standard for most projects
 - More may be required for riskier ventures, such as restaurants and recreational enterprises (35%)
 - At minimum, 10% actual cash is required as part of the typical 20-35% down payment for SBA loans—usually cannot be borrowed money
 - Additional down payment required may be made up with equity in other assets; long term loans will require real estate equity



Things that make your lender happy ...

- Seller-financing does not count towards the SBA's 10% cash-down requirement
- Be prepared to put up your house!
- Collateral discounting previously discussed applies!
- Creditworthiness and relationship with borrower may impact requirement
- Good credit scores (>720)
- Profit on the tax return!
- Access to Working Capital (daily operations)



Things that make your lender happy ...

- Current Assets divided by Current Liabilities including current portion of long term debt
- Abundant collateral
- Equity (Assets – Liabilities) > Liabilities
- Adequate insurance to mitigate risks—property, life, health, disability, business continuation?
- Estate and succession plans clearly thought out and in writing
- Business agreements with partners in writing



Other tidbits ...

- Lenders can only base lending decisions information you report to the IRS. (beware of CASH sales)
- Clients must balance the desire to pay minimal taxes against the need to obtain current and future financing, including a cushion for growth.
- For a spouse's outside income to be considered in debt service calculations, spouse must usually be a co-borrower or guarantor.
- Poor personal credit history of the spouse can hamper the business's ability to get credit or increase rates.



Other tidbits ...

- Clients must balance the desire to pay minimal taxes against the need to obtain current and future financing, including a cushion for growth.
- For a spouse's outside income to be considered in debt service calculations, spouse must usually be a co-borrower or guarantor.
- If you have to be late on something, don't let it be a payment to the bank or something that's reported to the credit bureau.
- Bankruptcy is at least a 7-year problem.
- Late payment of taxes, particularly payroll taxes, is a MAJOR problem.



- All lenders are not the same
- Research various lenders, ask questions.
- Establish a relationship with your lender
- Different loan programs
 - Ohio Grow Now Program
 - SBA Small Business Administration
 - Gap Financers





Loan Package Checklist (1)

_____ Business Plan

_____ Market Research (where applicable)

_____ Resume of Owner(s) and Key Management

_____ Sources (bank loan, owner's cash equity, etc.) / Uses (building, inventory, working capital, equipment, etc.) of Funds include

Annual Debt Payment of any Loans

_____ Copy of Partnership Agreement, Articles of Incorporation, Articles of Organization

_____ Copies of Licenses, Permits, Trademarks, etc.

_____ List of collateral (with serial numbers where applicable), age, cost, current market value

_____ Personal Financial Statements for Anyone with 20% or more Interest in the Business

_____ Personal Federal Tax Returns for the Previous Three (3) Years for Anyone with 20% or more Interest in the Business



Loan Package Checklist (2)

- _____ Name, Address, Telephone Number of Business Attorney, Accountant, Insurance Agent, Business Consultant
- _____ Twelve (12) to Twenty-Four (24) Month Cash Flow Projection with Line Item Description
- _____ Three (3) years of Projected Annual Profit and Loss Statements
- _____ A Beginning Balance Sheet for Start-Ups or a Projected One (1) Year Balance Sheet for an Existing Business
- _____ Written Quotes on any equipment Purchases / Leases and / or Construction Costs
- _____ Copies of any Real Estate/ Other—Purchase/ Lease Agreements
- _____ Legal Description of Real Estate that is a part of the Business or to be used as Collateral
- _____ Recent Property Appraisals or Business Valuations
of collateral (with serial numbers where applicable), age, cost, current market value



Loan Package Checklist (3)

- ___ EPA Related Documents
- ___ Letters of Intent from Prospective Customers
- ___ Profit & Loss Statements and Balance Sheets for up to the Previous Three (3) Years
- ___ Interim (within the past 90 days) Profit & Loss Statement and Balance Sheet
- ___ Company's Tax Returns for up to the Previous Three (3) Years
- ___ Aging of Accounts Payable/ Receivable
- ___ Contracts with Customers
- ___ List of Customers and Percent of Business each account for
- ___ Favorable Letters form Commercial Customers



\$\$\$ Websites of Interest

- \$ Treasurer of Ohio www.tos.ohio.gov
- \$ Ohio Development Services Agency www.development.ohio.gov
 - Has a variety of bonds, grants, loans and tax credits that can assist Ohio companies as they grow and create jobs
- \$ Finance Fund www.financefund.org
 - Connects local small business owners and entrepreneurs with public and private funding to help spark community development and create jobs.
- \$ United States Dept. of Agriculture www.usda.gov
 - *USDA Farm Service Agency www.fsa.usda.gov
 - *USDA Natural Resources Conservation Service www.nrcs.usda.gov
- \$ Small Business Administration (SBA) www.sba.gov
- \$ Ohio Valley Regional Development Commission www.ovrdc.org
- \$ Southern Ohio Ag & Community Development Foundation www.soacdf.net
- \$ Economic & Community Development Institute (ECDI) www.ecdi.org



Informative Websites of Interest

The Ohio State University South Centers	<u>http://southcenters.osu.edu</u>
Business Development Network	<u>http://southcenters.osu.edu/business</u>
Ohio Small Business Development Centers	<u>www.ohiosbdc.ohio.gov</u>
The Ohio Secretary of State	<u>www.sos.state.oh.us</u>
Ohio Business Gateway	<u>www.business.ohio.gov</u>
Ohio Department of Taxation	<u>www.tax.ohio.gov</u>
Ohio Department of Agriculture	<u>www.agri.oda.gov</u>
Internal Revenue Service	<u>www.irs.gov</u>
United States Dept. of Agriculture	<u>www.usda.gov</u>
*USDA Farm Service Agency	<u>www.fsa.usda.gov</u>
*USDA Natural Resources Conservation Service	<u>www.nrcs.usda.gov</u>



Questions or Comments??

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