How to Finance the Un-Financeable Business

If I were to identify one KEY factor to accomplishing this daunting task, it would be to begin it with an open mind. Most people who have approached me over the years to do this, come to me with a picture in their minds of a bank handing them a big check to help pay old creditors or a new advertising campaign. In the mind of the entrepreneur they believe the bank sees this the way they do, "What an opportunity for everybody to make money".

What the bank actually hears is:

- *So you used/lost all your money and now you want mine.*
- *Not only that, but you plan on paying me back out of cash flow that my money will create since you don't currently have any cash flow of your own?*
- *So I'm supposed to believe that what you bet your money on and lost is now going to work.*
- *Hmmm let me think, NO!*

What this should tell you is that approaching multiple banks with your request will not suddenly provide a different result. Oh I know that you have been talking with a "banker" who says they can get this deal done. This is very common and many owners invest huge amounts of time counting on the banker who says they can do the impossible.

The truth is that this banker is usually nothing more than a salesperson dressed up to look like a banker. They play the numbers and know that if they bring in ten opportunities, one of them will be approved by the underwriters who actually make the decision not the banker.

The fact that nine owners walk away unbelievably disappointed is of little concern to the salesperson. They say they tried and we actually thank them for the effort of wasting our time when it wasn't a viable deal to begin with.

BEST CASE SCENARIO - So we know we have to do something different, but what is it? You are actually <u>selling</u> your company to the lender but the problem is that you don't get the chance to vocalize the sale. They simplify the process and take out all of your hype and enthusiasm by solely looking at what the numbers are telling them.

So here is the first key: make the numbers look as good as you can. What I am NOT saying is to fudge the numbers; what I AM saying is that many accountants use proper accounting methods, but not necessarily favorable methods. For example it is acceptable to use accelerated depreciation, but if the company has had recent losses, this will only decrease the equity reflected on the bottom line. There are also approved ways that your accountant can account for tax purposes and account differently on your financials. Unfortunately finding an accountant who understands all the nuances will require a bit of a hunt, but is totally worth it in terms of cleaning up your balance sheet quickly.

We know that cleaning up your car before attempting to sell it will always result in getting more money for it, or at least selling it faster.

That said you also have to pay attention to the glaring issues that will loom large in front of a lender:
Negative equity, insufficient cash flow to service the debt, excessive debt, the last year or two of losses.

There are also methods available to clean up debt which will be determined by the amount and type of debt. For example: there is a particular technique that will take all of your trade payables that are delinquent, lump them together, convert this "short term" debt into "long term" debt which is typically much more desirable, and perhaps even reduce the amount you need to pay back over the next few years instead of tomorrow. This can change the complexion of the balance sheet overnight.

For more on this subject see our white paper entitled, **"Making Your Business Attractive to Banks or Putting Lipstick on the Pig".**

MID CASE SCENARIO - Now we want to take a look at alternative ways to secure financing because there is an abundance of ways in which this can be accomplished. Banks are a good place to start if you qualify, but they don't do most of the financing for small businesses as their guidelines are fairly strict. As you go deeper into the list of choices for funding, the cost of money increases.

For example, leasing is a good alternative and a bit higher cost than bank financing. Also asset based lenders are an option. At the other end of the list is factoring or selling your receivables or credit card advances. These can run up into the 24% to 35% range and actually drive you out of business if you don't have a clear cut plan to make more with the cash this provides to you than what it cost you to have the cash available. If you haven't had spreadsheets run for you by your financial people on how this will happen, I strongly suggest that you not get caught up in this.

Here is a list of many of the available sources that are many times overlooked:

- Leasing
- Mezzanine Financing
- Venture Capital
- Private Investors
- SBA
- Other Special Government Programs
- Asset Based Lending
- A/R Financing
- A/R Factoring
- Credit Card Financing
- Purchase Order Financing
- Contract Financing
- Sale Leasebacks
- Hard Money Lenders
- Angel Investors
- Real Estate Commercial
- Real Estate Residential
- Partnerships
- Sale/Purchase
- Contract Financing

Knowing where to find these people can be problematic, and you would be smart to work with someone who has contacts in these worlds. The good news is that many of the higher interest players count on 3rd parties to bring them the deals and discount the rates for these people. True they mark them up again to make their cut, but usually only to about where the market would be if you could find these sources directly.

The reason it can be difficult is that a given resource only has so many dollars to invest at any point in time. For this reason the availability of money to lend can change on a daily basis. Someone who has money today may not have any tomorrow until they package their loans and sell them thereby raising more cash. Other reasons such as market condition and changes will affect availability of funds and their costs. This ebb and flow creates an ever changing playing field, and unless you are in touch with the players on a regular basis it will be difficult if not impossible to unearth them.

WORST CASE SCENARIO– What if you just don't look good on paper, have losses or bad personal credit? There are still choices so keep an open mind as to how you can get this done. If the rates are too high for those who are willing to fund you or you can't get anyone to even consider your deal, try one of these options.

Borrowing from those who have something to gain by seeing you in business is always a strong alternative to consider, but they must be approached properly to sell this. These are onetime chances, and a bad approach here will kill any prospects of a second attempt. Once they think they understand the offer, you will not be able to repackage it in their mind. I have had numerous clients who thought they could pull this off themselves only to find out they had ruined their only chance. With that caution in mind, I have been successful in every one of the suggestions I am about to outline for you.

Front line of defense is friends and relatives. If you are lucky enough to know somebody with money who has confidence in you and your endeavor this is a good source. HOWEVER if you are going to do this treat them like the secured party (just like a bank) they deserve to be. This does a few things for you. First it makes it easier to talk them into the deal by assuring them that they will be paid back ahead of everybody else in the worst case. Because they are "friendly", it gives you control over other creditors who may apply pressure for collections at any point in time. You could actually ask your friend to foreclose (friendly foreclosure), take back the assets they are secured against and sell or lease them to a new company. That'll neutralize threats overnight!

You can also talk to a key supplier or a few key suppliers who have a lot to gain by you staying in business. Show them exactly what you have spent with them over the past years. Translate that into what should be their profit margin and compare the loss of that to the gain of not only what they are owed, but future sales and profits. Depending on your numbers, it may even be sufficient to ask them to lump the outstanding amount you owe them into a note payable over the next 6 months to a year.
Again offer them a secured position IF NECESSARY to assure them of repayment. The tricky part here is to know if they really need your business and if they do you may be able to talk them into new credit that is hinged to the old debt repayment. In other words for every dollar of new credit, the repayment amount will be $1.10 with the dollar going to pay off the new line and the 10 cents towards the old debt. If you have a lot of creditors who are owed money, I would suggest a more broad sweeping solution.

For more on this and other solutions see our white paper, "Creative Financing for Your Business".

If you have a line of credit with a bank, think about asking them to convert it from a line of credit into a term note and then reopening a new line. This will help your cash flow and take off the immediate pressure of bank payments that are past due.

See the white paper on, "9 Ways to Create Cash Flow".

What most people fail to see here is that you have created a brand new loan for a business that wouldn't have qualified under normal circumstances.

There are many more methods depending on the particulars of your business, but for the purpose of keeping this to a white paper length our space is limited. Please feel free to contact us for more ideas and information.