



Today's Sayings

Given a choice between building your business on large debt or facing a firing squad, choose the firing squad. There is a chance the firing squad may miss.

In business today, too many executives spend money they haven't earned, to buy things they don't need, to impress people they don't like.

Sayings

- Why do banks charge you a “non-sufficient funds fee” on money they already know you don’t have?

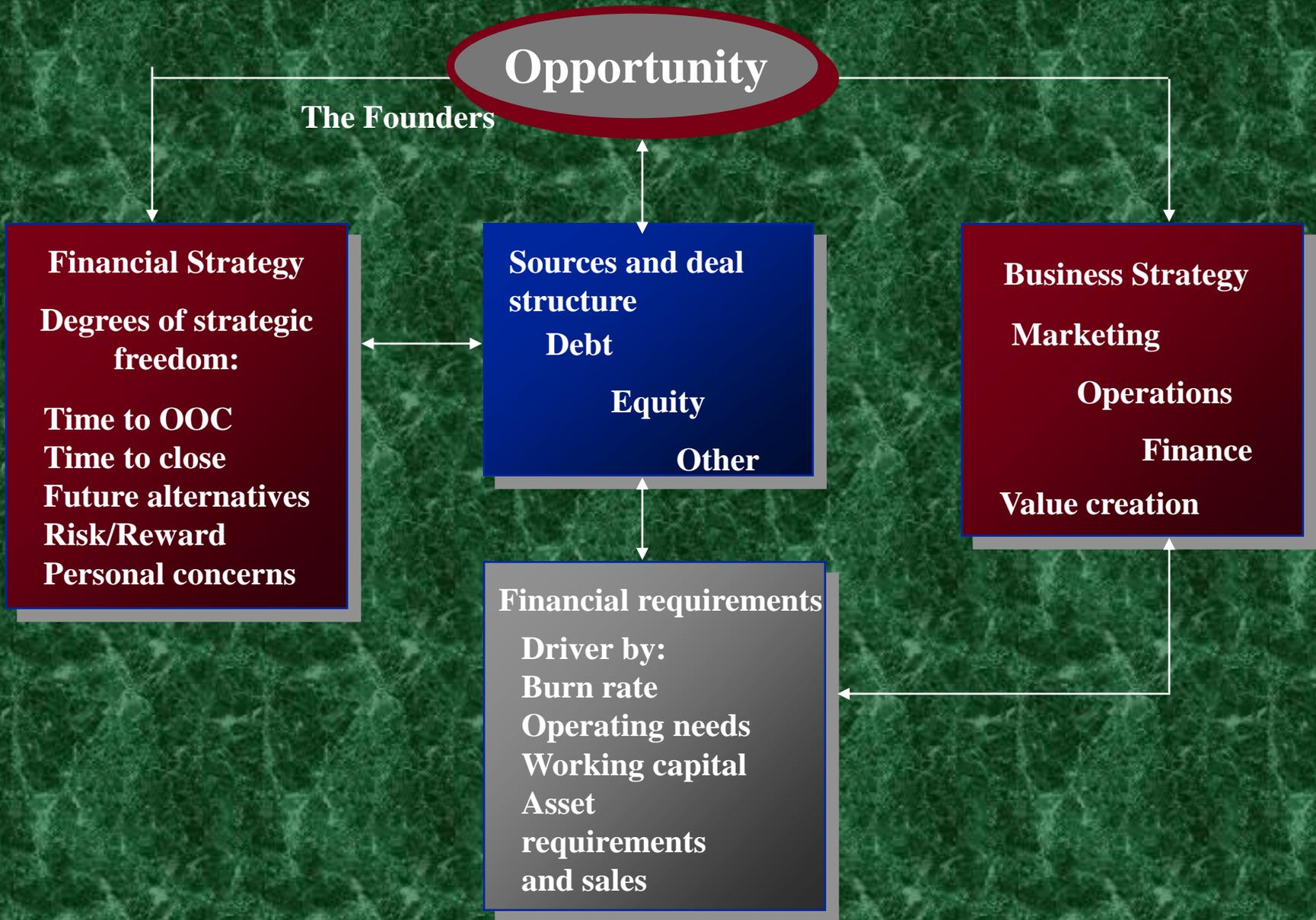
Identifying Sources of Financing

- Understand sources and implications of finance
- Understand how to contact and deal with finance sources
- Understand differences between equity and debt
- Review government finance programs

Financial thought of the day

- The commentators have it all wrong. Look on the bright side. The world economy is not in a period of negative growth. It's in a period of positive collapse! That's why the Great Depression was so great, after all. What's positive about this depression is that it is clearing away a generation's worth of mistakes, misallocations of resources and misplaced confidence.

FINANCIAL STRATEGY FRAMEWORK



How to Formulate Financial Strategy

1. Start with opportunity--not the need for cash
2. Formulate business strategy appropriate to capture the opportunity
3. Define the cash need:
 - a. Assets
 - b. Working capital
 - determined by free cash flow
 - burn rate -- out of cash -- time to close
4. Then formulate financing plan

Remember the \triangle between corp. and E finance --cash is #1

Determine Capital Requirements

- First do a marketing plan
 - sales and profit goals
 - marketing and sales plans
- Construct financial proformas
 - P&L's, balance sheets, assumptions
 - cash flow analysis

New Venture Financial Issues

- Determine what stage you are in
 - prestart, start-up
 - early stage, mezzanine
- Determine the quality of the borrowing base
 - the big idea - USP
 - assets
 - cash flow
 - receivables

Craft Fund-Raising Strategies

- Personal objectives and needs
 - hobby businesses
 - side-line businesses
 - your livelihood
 - EMPIRE building
- Friends, family, relatives
- Debt vs. equity sources

Questions to answer

- How much control do you need?
- Who do you want to marry?
- How are you going to spend the money?
- How will you maximize the capital?
- Better to bootstrap or use OPM?
- Are you prepared for the capital hunt to become a full-time occupation?

Finding the right sources of financing is
a lot like choosing between two blind
doors

-with Tigers behind each.

R Hirasawa

Equity Tigers

- Investors have a universal motive - to make money
- Investors are always interested in knowing specific exit strategies
- What is most important to an equity investor?

Equity Tigers

- Friends, Family, Relatives
- Private Investors
- Angels
- Venture Capitalists
- Corporate Investors

Business Plan Statistics from a Venture Capitalist

- 4 out of 5 are discarded within 15 minutes
- Of the remainder, 4 out of 5 are read for an hour and then thrown out
- Of the remainder, 3 out of 4 are turned down after meeting with management
- Of the remainder, 1 out of 3 will be funded

The better you see the risks
through the eyes of the investor,
the better your chance of funding.

Different Investor Types

- Nervous
- Back seat drivers
- Investors who like their hands held
- Investors with hidden agendas
- Your ideal investor

Angels

- Usually do not like start-ups
- Make high (>40% annually) returns
- Take an active interest
- Concerned most with quality of management
- Like businesses they are familiar with
- Invest on average about \$50k apiece per venture

Debt

YOU WISH TO JOIN MY ALLIANCE TO DESTROY THE UNIVERSE? WHAT SKILL DO YOU HAVE?

YEAH. WE CAN MAKE LOANS TO EVERYONE IN THE UNIVERSE. IT'LL IMplode.

BANKERS.



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Debt Tigers

- Lenders share your business risk for a set fee
- Will only loan to those they consider trustworthy
- Love qualified guarantors
- Do not really care about your business. They will secure their loan to eliminate their risk

More on Debt Tigers

- They like to see that you have a large retirement account balance
- They will only loan to those who appear not to need it
- They will never come through on their first commitment



"Here, perhaps you'd like one of our brochures on how we don't give loans to people like you."

Debt Tigers

- Personal loans
 - FFR, credit cards, home equity
- Debt Capital
 - trade credit
 - commercial banks
 - finance companies, savings and loans
 - factors
 - leasing companies
 - insurance companies



TURNING RECESSION
INTO DEPRESSION

PROJECT FUNDED BY
Your Grandchildren
and
Great-Grandchildren



USDOT
WAGON

Be Aware

- Traditionally credit card financing has been the number one choice of entrepreneurs. The new (2005) bankruptcy law has made it much harder to discharge credit card debt and must be factored into this decision.

Factors that reduce available capital

- Compensating balances
- Discounted interest (in advance)
- Lags in check clearing
- Securitization formulas

Factors that increase costs

- Points
- Application fees
- Commitment fee
- Due diligence costs, legal costs, UCC filings
- Prepayment fees, termination fees
- Monitoring and audit fees
- Unused line fees
- Float days

Do not overlook combining both
debt and equity

Government Tigers

- Federal
 - SBA
 - grants
- State
- Local County, City

Dealing with the government

- Would you rather be focused on your business, or would you rather be focused on the laws, regulations, policies, etc. that the government has set up regarding your business?
- The more you rely on the government, the more you better understand the following slides.
- Note – these are explanations of the new “Small Business Jobs Act”. The actual law is much harder to read.

Small Business Jobs Act of 2010

- The bill increases the Microloan Program maximum loan amount to \$50,000 from \$35,000.
- It also increases the limit on the government's participation in Section 7(a) small business loans to 90% from 75% or 85% for all Section 7(a) loans regardless of loan amount.
- The new maximums under the SBA's 504 Program are tiered in relation to the borrower's plans to use the capital to support federal government priority goals and projects, mostly in the energy and manufacturing sectors
- The reduced fees for SBA loan guarantees enacted by the American Reinvestment and Recovery Act of 2009 (ARRA) are extended to Dec. 31, 2010 (from Sept. 30).

Small Business Jobs Act of 2010

- Up to \$7.5 billion in low-interest refinancing is available under the SBA's Local Development Business Loan Program. Up to \$7.5 billion annually is available for loan refinancing for two years after enactment for qualifying loans. Qualifying conditions include meeting job creation and retention goals and providing collateral valued at least 125% of the amount financed.
- Creates a floor plan refinancing program, under which the SBA can guarantee open-ended extensions of credit to small businesses if the loan is used to purchase certain eligible retail goods for resale.
- The maximum amount of express loans under Section 7(a) of the Small Business Act is increased to \$1 million from \$350,000 for one year from the date of enactment.

Small Business Tax Relief

- *Section 179 expensing and bonus depreciation.* The bill increases the maximum amount a taxpayer may expense under IRC § 179 to \$500,000 and increases the phaseout threshold amount to \$2 million for tax years beginning in 2010 and 2011. The first-year 50% bonus depreciation available under IRC § 168(k) is extended for one year to apply to property acquired and placed in service in 2010 (or 2011 for certain long-lived and transportation property).
- The bill amends IRC § 1202 to increase the exclusion from gross income of gain from the sale or exchange of qualified small business stock from 50% to 100%, and the minimum tax preference does not apply.
- The carryback period for eligible small business credits under IRC § 38 is extended from one to five years.

Small Business Tax Relief

- For tax years beginning in 2011, the bill provides that for purposes of computing the section 1374 built-in gains tax, the recognition period is the five-year period beginning with the first day of the first tax year for which the corporation was an S corporation.
- The bill increases the section 195 deduction for trade or business startup expenses from \$5,000 to \$10,000 for tax years beginning in 2010.
- The bill limits the section 6707A penalty for failure to disclose a reportable transaction (that is, a transaction determined by the IRS to have a potential for tax avoidance or evasion) to 75% of the decrease in tax resulting from the transaction.
- The bill removes cell phones from the definition of listed property.
- The bill allows self-employed individuals who deduct the cost of health insurance to take the deduction into account in calculating net earnings from self-employment for purposes of SECA taxes.

Much of the decision of equity vs.
debt is tax driven

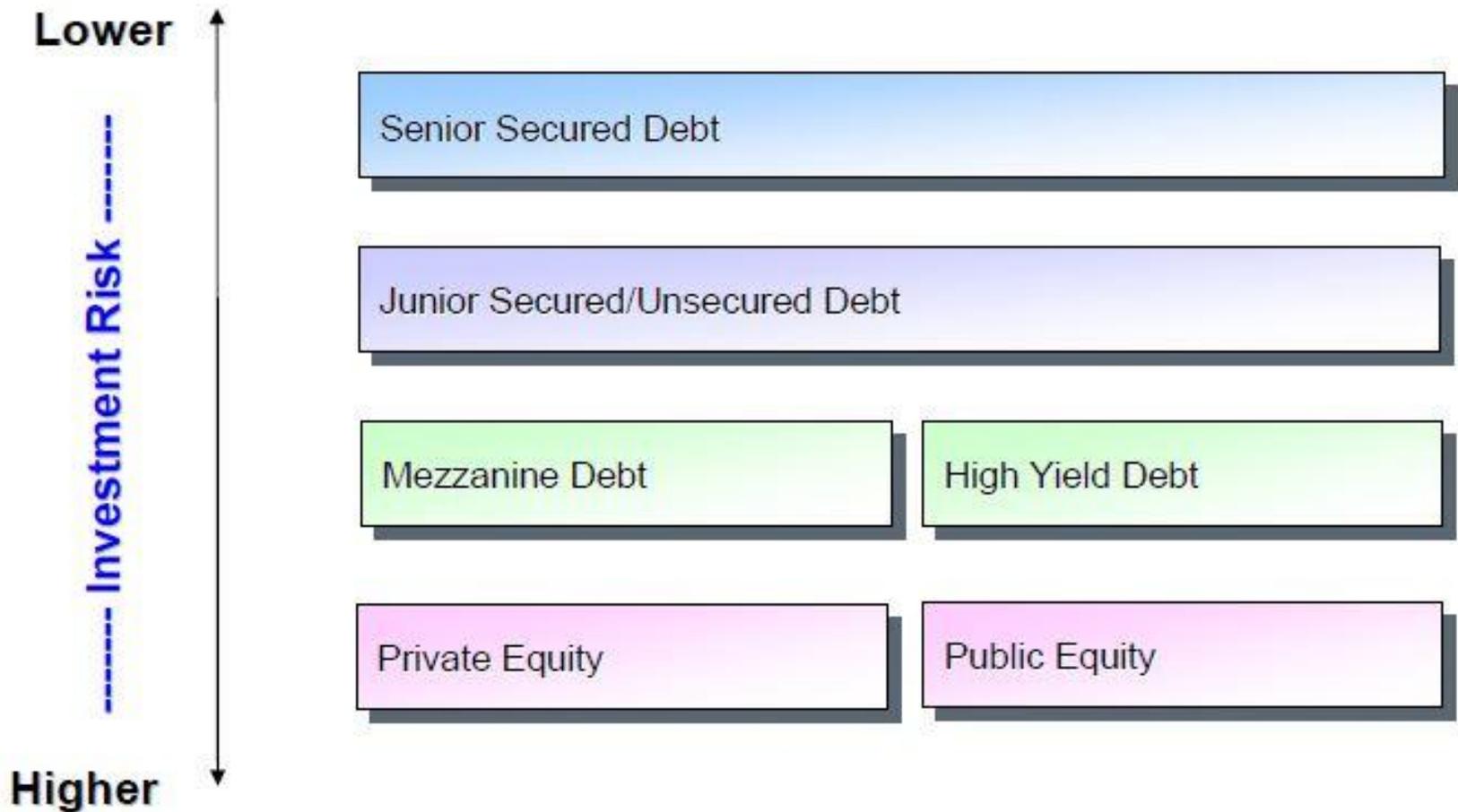
Advantages of Equity

- More flexible
 - can adjust rate of return
 - owners cannot force company into bankruptcy
 - owners are less likely to sue over complaints
- Possibility of ordinary tax losses (debt losses of individuals may be capital losses)
- Capital gain treatment for appreciation
- Roll over of gain possibilities

Advantages of Debt

- Increases leverage for owners
- Deductibility of interest
 - Dividends are double taxed
- Non-taxability of principal repayments
- Justification for accumulated earnings
- Debt losses are ordinary losses if business debt

Financing Options



Indicators of Debt

- Unconditional promise to pay
- Higher priority than equity
- Debt to equity ratio
- Convertibility
- Proportionality
- Documentation and actions are very important

The 4 C's of Borrowing

- Credit history of borrower
- Collateral to secure loan
- Cash flow history and projections
- Character of borrower

Don't approach your best prospects first.
Call on your long shots and practice
giving your presentation to them.

When you are rejected for financing:

- find out why

- ask for suggestions of other sources that you should pursue

Other sources of money

- Equipment leasing offers a variety of ways to make bad capital investments
- You always pay for the flexibility in a lease

How much should you ask for?

- Always ask for more than you need
- Never ask for more than you need

To get money you need to:

- Have the ability to project, and then perform to plan
- Differentiate between fact and assumptions
- Have the ability to deliver. Plans cannot keep changing.
- Have a story built on correct facts and have a reasonable probability of being executed (the story, not you)

The legal documentation

- Read and understand the impact of every word in your document
- Do not waste time with non-sensical revisions
- Be prepared to spend a lot of time with lawyers
- Do not sign until it says what you want it to say

Don't forget the due diligence
process!

Time runs a close second to cash on every entrepreneur's list of scarce resources. Do not waste valuable time thinking about raising venture capital or debt until you convince yourself that your venture will generate substantial wealth. A successful financing hunt will normally take at least 6 months (this is from before the 2007 and 2008 market crashes) from start to finish. You must have both a good opportunity and a substantial desire, or the process will eat you alive.

Sobering Thought

More than 80% of the fastest growing companies were financed solely by the founder's personal savings, credit cards, second mortgages, customer advances, extended terms from vendors, and other bootstrapping techniques.

Final Thought

- Most entrepreneurs overlook the very best source of cash - the cash they already have

