payroll financing solutions
QUICK BUSINESS FUNDING

White Paper: What Funding Options are Available for Business Owners

One of the most important actions a business owner can do is make sure they have funding in place to help their company in good times and bad. However, depending on the phase you are in your business, it is important for you to know your funding options. Below are the various funding options available.

Payroll Financing or Payroll Funding

Payroll Financing is an alternative lending option used for short term emergency funding to help companies free up capital. This financing is intended to help business owners pay its employee's until the business can get back on track during an unforeseen expense or large increase in sales. The financing can be spread out for as long as 6 months or shorter if the business owner requests. In a short term loan situation Payroll Financing is the cheapest form of professional loan. Payroll financing companies will look at your companies past success and current viability to determine if funding can be issued. The Payroll Financing Company can often make a decision in 24 hours or less and can be very flexible in terms of when you can pay off the loan with no penalty. Often, business owners who use Payroll Financing are just trying to solve a temporary funding problem. This type of loan is not used for startup businesses and typically requires at least 3 years in business.

Pluses

Emergency funding used to pay your employees during unforeseen company event
Keeps your business going without disruptions until other financing can be arranged
Cheapest cost for short term financing
Doesn't tie up credit
Super-fast approval decisions in 24 hours or less
Unlike banks, more open minded in approval criteria
Willing to issue funding up to $100,000
Not tied to long term funding commitment like with a Traditional Factor

Negatives

More expensive than a bank loan
Your business has to prove the funding can be paid back
Should not be used to fund an unprofitable business
Need to be in business 3+ years

Commercial Line of Credit thru a Bank

In most cases, unless you need the loan for only 90 days or less or only once every 2+ years, a commercial line of credit thru a bank will be the cheapest way to borrow money. The line of credit will take you 4-12 weeks to establish and the bank will look at your business financials, personal credit, and collateral. Collateral might be your home, cash on hand or other liquid assets and this will be used to back up the loan in case of default. The bank will file a UCC (Uniform Commercial Code) which will show up on your credit report identifying assets in case of a default. The UCC also allows other financial institutions such as equipment leasing companies to know your assets are assigned and limits what others will lend you. Most banks will want reviewed/audited financials from your accountant yearly which will cost you extra to get done and your bank will charge you a yearly fee to keep the line open. The bank will ask you for how much money you want the line to be for and that amount will need to be justified based on the business history and your collateral. Covenants are what banks put in place to measure should you keep the loan or if you want the line of credit increased and will be reviewed quarterly or yearly. Banks are of course the most risk adverse so they will want to make every effort in their due diligence to ensure you can pay the loan back.

Pluses
Cheapest form of loan in the long run
Protects you against emergency money needs
Helps you fund accounts receivable until clients pay you
Can be used in any way you deem necessary
Negatives
Substantial increased expenses for review or audited financials
Yearly fee for keeping the line of credit open
Ties up available line of credit for other loans such as equipment leases
Takes 4-12 weeks to obtain with extensive owner involvement in process
Spouse may not be happy with personal assets being assigned
Hard loan to get until you are already successful
Yearly review and approval process for renewal
Restricts business decisions based on covenants
Will need to be in business for 3-5 years before a bank will approve line

Traditional Receivable Factoring

Factoring is actually a very old form of financing that has the benefit of being tied to your sales or "Receivables". If your sales are there, the financing is there. Factors are designed to limit their risk by funding up to 90% of your invoices for 90 days. A Factor will start off by contacting your clients to make sure that the invoices are real and that your client is credit worthy. In the due diligence phase, the Factor will ask you details about your business.

Factors tend to specialize in certain industries. Factors have the right to reject a client you are working with or that you want to work with and if your client hasn't paid the Factor in 90 days, you will have to give the Factor back their advanced money unless it is a non-recourse Factor. A Factor will charge a yearly fee which can be substantial. In 3 cases, we saw a yearly fee of $15,000-$20,000 for a $2 million business plus a high interest rate for each invoice they fund. Factors are not cheap and can cost 3-5 times what a bank charges. Factors are really looking for a long term relationship and once a business gets involved with a Factor, it is hard to move away from the Factor. If a business feels they will need the money for 2-3 years and you are unable to get a bank line of credit, then one option is to use the Factor for 2-3 years and then line up a bank to get rid of the Factor.

Pluses
Unlimited funding. You get the business, they will fund your receivables as long as client is credit worthy
Negatives
Very expensive funding solution
Factors want a long term relationship with you
Factors will call your clients which may worry some clients about your business
Yearly fee even if you don't use Factoring that much
Factor might refuse to fund certain of your clients
Factors advance only 80-90% of your receivables. Problem for tight margin businesses.
If you clients pay >90 days you could have a funding problem
Will file UCC against your company affecting other financing
Hard to move away from Factors down the road
Can take 4-6 weeks to start funding
Your clients checks are going to Factor and then to you (fraud potential)

Merchant Funding or Merchant Cash Advance

Merchant Funding companies advance money to companies based on a percentage of the monthly amount of your past business credit card transactions. You need to already accept credit cards in your business. Merchant funding companies are a form of factoring and are often independent organizations that will look at your business credit card transactions to advance you money based the history of monthly receivables and how many transaction are done daily.

Pluses
Instant cash
Automatically sends you money
You are not personally liable to repay if you business goes south
Easy to obtain
Minuses
Very expensive
You need to already accept credit cards
Need to have a history of credit card transactions
Will want to see lots of small transactions and not larger transactions
Really only used for retail industry
Amount they are willing to loan might be to small to help your business

Home equity loan

Some business will get a home equity loan and will use that loan for the business when they need it. A home equity loan is based on how much equity you have in your home and one would get this loan mostly through a bank. There might be an appraisal needed which would cost $1,000-$2,000 plus a loan application fee. This loan might take 2-6 weeks to obtain depending on the amount you are asking for.

Pluses
Inexpensive form of a loan
Easier to figure out how much is available
Can keep open yearly for a small amount of money
Negatives
Can have detrimental effect on your relationship with your spouse
Spouse might be required to cosign loan
Might take too long for you to get loan for your needs
If you don't pay it back, your home is at risk

Refinancing of your home

Your home might have a considerable amount of equity or you might be farther along in its payment schedule. You might be able to refinance your home and use that capital for you business Refinancing of a home might take 4-6 weeks and you might be able to get more money out in this type of loan verses a home equity line of credit.

Pluses
Inexpensive form of loan verses say a Factor
Negatives

Can have detrimental effect on your relationship with your spouse
Spouse might be required to cosign loan
Might take too long for you to get loan for your needs
If you don't pay it back, your home is at risk
The amount might be limited

Friends and Family

If you do have family and friends with significant money and you really need the money for an emergency loan, this might be good alternative.

Pluses
You get the loan to tie you over in emergency situations
Could be paid back with little to no interest
Negatives
Could cause a problem in your relationship
Your friends/family might not have the money
You may not want to reveal you have a problem/need help

Angel funding

Angel funding is when you agree to give up a percentage of your company in exchange for someone investing in your company. Contrary to most people's perceptions, Angel Investors are looking for the company to have an exit strategy where you sell to either another company, or venture capital firm eventually. Most angel funding investments are in the $100k to $1 million range and the investors are looking to get a 10 times return on their money when you sell. Angel funding deals can take 6 months to 12 months to finalize resulting in a huge time commitment from the owner. It is estimated that only about 10% of companies seeking angel money get funded.

Pluses
Good investment capital to grow the business
Good strategic investors can help you grow your business better
Might give your business a competitive advantage
Your strategic direction might require this larger amount of capital
Negatives
Takes a long time to raise the money
Management will not be able to focus on building business during this phase
Lots of legal bills to finalizing agreement
A lot of pressure on owner to deliver
A lot of energy will be spent by owner/management team
Owner will need to make decisions in concert with investors from now on
Selling company in the future will be a committee decision but investors will want you to sell
Giving up equity in your company

Venture Capital

Venture capital is the most misunderstood way for companies to raise capital. VC's are looking for established businesses that have already achieved sales in the $10-$30 million range and have enough growth potential to go public or to be sold to a bigger company. Like an Angel investor, VC's are looking to get their money out thru an exit strategy and not thru organic growth.

Pluses
This is the big time
Owner is going to get a big pay day
New professional experiences
Negatives
Most VC's will want to replace the owner and bring in a professional team
Owners job will change
Entrepreneurialism is over as far as what you have done so far

Credit cards

Many businesses have been run on credit cards. If you are looking for a small amount of money, like $2,000, $4,000 or less than $10,000, you might be able to get this amount from a cash advance on several cards. However, over the years, this practice had been harder to do. Credit card companies will look at your credit score to approve your advance and having a large balance will greatly affect your ability to borrow money. Some owners will fill out numerous credit card applications but this takes a ton of time and is extremely challenging to manage.

Pluses
Access to a small amount of capital
Quick answers
Negatives
Affect your credit
May not be enough money top help you
Affects credit score
Takes a lot of your time
Very expensive

This white paper is written by the Stephen Halasnik and Keith Giovannoli owners of Payroll Financing Solutions who have built 8 companies over the last 18 years. Payroll Financing Solutions provides quick Financing to good companies when an unexpected expense or an increase in sales occurs. Please call us at any time at 862-207-4118x502 or e-mail us at info@fundmypayroll.com and we would be happy to helpor answer any questions you might have.