

How to Obtain Funding For a New Business

Government Funding

The [Small Business Administration](#) (SBA) exists to help promote the startup, growth, and success of small businesses in America. It was created as a result of the Small Business Act in 1953 and has helped millions of entrepreneurs get started on the path of owning their own business. To help fund small businesses the SBA provides some basic services. Under the 7(a) Loan Program, they work in conjunction with local lenders to guarantee loans to small businesses. They also work with local non-profit organizations to provide microloans to assist in the startup of small businesses.

Microloans

The SBA also makes [microloans](#) available through local non-profit intermediaries. The size of these loans cannot exceed \$35,000, with the average loan being \$10,500. All loans are provided on a local level through approved institutions to promote a better interaction between lenders and borrowers. The maximum allotted time for repayment is six years, with the rare exception made by the lender. The local lenders handle all eligibility and acceptance requirements.

The 7(a) Loan Program

The primary goal of the [7\(a\) Loan Program](#) is to provide small businesses with startup capital, and to help ease the risk incurred by banks in dealing with new businesses. Under the program, a potential borrower applies for a loan from the lending institution of their choice. The banks loan the money out and the government will guarantee a certain percentage of the loan if the borrower defaults on the repayment. Funds are available for those who qualify based on their current business status, collateral, character, credit rating, etc. The loans must be for a for-profit business and the borrower must be in a position to repay the loan. Those with the means to provide their own funding are ineligible for SBA loans. Loans are provided for the use in purchasing buildings, equipment, working capital, short-term capital, refinancing, and the outright purchase of a new business. Loans may not be used to pay back taxes, or to finance any unsound business practice or venture.

Quick Facts About SBA Loans

- **Maximum amount loaned and guaranteed is \$2 million and \$1 million respectively.**
- **The allotted time for repayment is up to 25 years for real estate and up to seven years for working capital.**
- **The amount guaranteed on each loans varies and can be up to 85% on loans of \$150,000 or less, and up to 75% on loans in excess of \$150,000 with a maximum of \$1 million guaranteed.**

More Information: <http://www.sba.gov>

Commercial Banks

Conventional Loan

In a conventional loan, entrepreneurs can usually borrow up to \$250,000. Monthly payments are made back to the bank to pay off the loan. These payments include interest and principle values.

Lines of Credit

A line of credit is an amount of unsecured short-term funds that a bank will make available to a business over a period of time usually a year. It is a revolving line of credit that has no fixed maturity. The entrepreneur pays interest for the amount used.

Equity Lines of Credit

This is a form of revolving credit that can be as high as \$250,000, for which the borrower's residential or commercial real estate serves as collateral.

Insurance Companies

Policy Loan

A policy loan allows the person to borrow up to 80% of the surrender value of his/her life insurance policy. The policy is assigned over to the insurance company as security against the loan. When the loan is repaid, all rights to the policy revert back to the individual.

Equity Financing

Partners

A partner is one of the quickest and easiest ways to raise up money for your new startup business. A partner is someone who will own part of the business and share in the profits and losses of the business. By bringing in one or more partners you automatically obtain access to one of more people who could be putting money into the business without the need to go to a bank or the government to obtain a loan.

The advantage to having partners is that you don't have to pay interest or have a bank payment that you're expected to make at the end of every month. If you have a tough month and the money didn't come in as usual there won't be a bank pounding on your door trying to close you down.

The disadvantage is that you're giving up some of your business. The more partners you bring in the more of your business you don't own. The more partners the more the profits are divided up among them.

Partners are a great way to raise money for a small business because not only do they bring in the extra money you may need to get going, but they bring in another worker to help out and more insights that might be missed if you were trying to go about things on your own.

Venture Capitalists

Venture capital firms are groups or people that invest in new companies or even companies that wish to expand and grow. There are over 600 venture capital firms currently operating in the United States. Venture capital firms are a great way to obtain money, but the process is incredibly difficult and less than 10% of all businesses that apply are actually funded.

The most important thing you must do before going to a firm to raise money is to write your business plan. Venture capital firms want to see exactly how you plan to run your business and what you're going to do to make sure that it is a success and they'll make money with you. A well thought through business plan takes much time and energy to fully express your business and capture the attention of these firms. As well as a business plan it would be wise to talk to a banker and a lawyer you can trust to make sure that you're getting a fair deal and make it through the legal network.

The average investment made by venture capital firms is between \$1.5 and \$2 million ranging anywhere between \$23,000 and \$50 million. Most start up companies don't require this much initial investment. Roughly 60% of start up businesses required less than \$50,000 to begin. It also takes on average up to eight months for one of these firms to reach a decision. So, if you need money quick, venture capitalists aren't the best way to go.

In exchange for their money, you give them ownership in your company. Depending upon the amount needed and how good they think your business idea is the firm will receive a percentage of the company that they hope to sell out on 5-10 years down the road for more than they put into the company in the first place. The firms usually don't take an active role in management.

If your company is involved in state of the art technology, growth industries, or essential services, venture capital firms like to see what you have. Rarely do they take time to invest in retail firms that have a harder time being successful and a slow growth rate. Firms want to find a company that will grow fast so they can get their money back quickly.

Angels

Angels work a lot like venture capital firms, but on a smaller and more intimate level. Angels are wealthy individuals, usually entrepreneurs themselves, who like to invest in small, start-up companies. The usual investment made by an angel is somewhere between \$20,000-\$50,000 which is more around the ballpark for most start-up companies today.

Like venture capital firms, when an angel invests money into your business it isn't a loan; you don't have to pay it back. The angel will receive equity in your business and own a certain percentage you both agree upon.

The best advantage about angels is that they've done this before. They have great experience and many connections that can help your business to grow into new areas and expand much quicker. This experience and the contacts can often be much more valuable than the money they actually put into the business.

Angels are the most advantageous source of funding for your business as an equity investment. They can help you more than a venture capital firm can because they're right there with you and want to see you succeed. Most angels aren't doing this for more money, but to help people do what they've done before and keep the system that made them successful in the first place going.