Shopping for Capital

Part 2: Alternative Approaches to Finding Capital

By Suzanne Boles

Finding financing for your business can feel a bit like entering the Dragon's Den. Once you've looked at all the traditional financing options including your banker, family and friends (detailed in the article "A Financial Primer for Franchising," *FranchiseCanada* November/December 2008) you might need to stretch a bit further.

If you're toying with negotiating a percentage of your business in return for an infusion of cash from venture capitalists on TV, don't jump right away. There are other options.

Social Capital Partners (SCP)

President Bill Young founded this innovative company in 2001. Initially, SCP worked with non-profit organizations looking to start up a business and willing to employ people on social assistance. After five years SCP felt the model was successful, having a positive impact by providing 200 jobs to people who might not otherwise have been employed, but they wanted to do more. They began investing in franchises because the risks are lower than independent start-up businesses.

Young says franchisees looking for an investment from SCP must "agree to hire 40 to 50 percent of their employees through agencies that help people who face employment barriers," adding, "Our commitment to the business owner is that we will find them a job-ready pool of candidates to choose from. So if we don't deliver on our commitment, they don't have to deliver on theirs."

Maximum amount of financing available from SCP is up to $300,000 per franchise but the actual amount will vary depending on the needs of a particular franchisee. A bonus, this money can be used to finance most of the "unencumbered" capital required to purchase a franchise, something that banks don't generally don't provide loans for.

SPC often works with the franchisor to determine the typical financing needs of their franchisees, and develops a program suited to their business model. "Then we'll sit down with the individual franchisee and make sure they understand and are comfortable with the social commitments that come with our financing package," says Young. SCP will also customize the financing to suit the franchisee's needs.

SCP outlines the process and benefits on their website, www.socialcapitalpartners.ca, under the 'Franchise Strategy' heading.

Factoring the numbers

Liquid Capital Corp (LCC) is a franchise in itself, with locations in the U.S. and Canada and provides funding through "factoring" (also known as accounts receivable financing). Brian Birnbaum, one of company's three founders, and Director and President of LCC Canada, explains that factoring "has been around since the Roman Empire, but started in Canada in the mid-1920s."

Factoring is the selling of outstanding invoices or receivables at a discount to another company that assumes responsibility to collect the receivables, which provides quick cash back to your business.

Birnbaum gives the example of a franchise staffing company with $25,000 start-up cash. To get the business going they need to phone a list of potential clients. In the first

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week they place five employees and pay each $1,000. By week five they've used the $25,000 but haven't received their first receivable so they don't have the money to pay their employees. That's where LCC comes in.

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LCC purchases credit worthy invoices from clients and collect the money owed by the client's customers. Once the goods and/or services are delivered, LCC advances the client 75 to 85 percent of the invoice up front. After collection, LCC pays the rest of the invoice, minus their fee. For businesses offering terms of 30 days or more, factoring eases their capital crunch and allows them some cash to expand their business and get through slower times in their business cycle.

Not all businesses are eligible for LCC services and criteria is based on various factors so contacting the company is the best way to find out if your franchise will qualify.

Business Development Bank of Canada (BDC)

The BDC is often another alternate option for franchisees looking to finance their franchise. The BDC is a term lender offering a wide range of financing options. Interest rates can be slightly higher than banks depending on the risk of the transaction, but financing can be for business expenses that banks are more reluctant to finance. BDC offerings include term loans to purchase land, buildings and equipment, working capital loans to top up short-term financing or lines of credit. Its venture capital group provides funding for any business that is being innovative (e.g. product development or new items to market) as part of of their expansion or growth.

Mary Gagliardi, Vice President and District Manager, Southern Ontario BDC, says solutions can be "tailored" to the needs of the business owner, from those who are in the start-up phase to the "transition loan," which can be used by anyone who is ready to sell their business.

Similar to traditional banks, BDC likes to see documented information – financial statements, executive summary, and information

about the business management team, or a full business plan. However, the documentation they require is not standard as every scenario requires a different level of reporting. Gagliardi says BDC does not have a set percentage for loans. "We tailor every solution to the client…We can be flexible in putting the package together that is unique to the client, based on their needs."

Gagliardi adds most people aren't aware that BDC also offers fee-based consulting services including financial consulting, human resources and more.

Advice from the experts

Speaking of consulting, sometimes the best thing to do when entering the financial arena is to sit down with an advisor to see what your options are. BDO Dunwoody can help there.

"BDO Dunwoody LLP is a national accounting services and advisory firm that offers breadth of expertise and innovative thinking to clients in over 95 offices across Canada… The firm provides clients access to world markets through its membership in BDO International," says Rick Chittley-Young, a principal in the Oakville office of BDO Dunwoody LLP, and Chairman of BDO's National Franchise Group. He also heads the Toronto region's Franchise Services Team.

Chittley-Young details what banks are looking for, when it comes to financing your business, the BDC, and even venture capital investments. He goes back to the ABCs of financing with solid advice about support from franchisors, the importance of the business plan, and the importance of consulting an accountant "who can help to calculate start-up costs, determine when the franchise is likely to be profitable and what kind of financing would be most appropriate."

Asked about the pros and cons of alternative financing he says, "It really comes down to affordable financing: it's important to carefully evaluate capital requirements and carefully match them with the appropriate financing. A new franchisee doesn't want to run out of cash but doesn't want to be paying higher fees and interest than absolutely necessary since these can also drain cash flow."

And if you're still thinking of entering the Dragon's Den, Chittley-Young offers a sound piece of advice. "If a franchisee intends to give up some equity in return for capital, it's important to consider how much control of the business they feel comfortable giving up."