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May 2016

The Monthly Resource Guide For Startup Businesses

# NEW BUSINESS

## MINNESOTA



# Money

## Unexpected Sources

### Special Report

Money is the lifeblood of any business. This issue explores alternative ideas to manage, grow and uncover revenue that many new and small business owners may not be aware of. New Business Minnesota presents these experts to help show you the way: **Pam Krank**, The Credit Department Inc. on Credit Management; **Lesley Farmer**, KLC Financial Inc. on Equipment Leasing Alternatives; and **Rochelle Hilson** and **Kristin Erickson**, **North Mill Capital** on Factoring Invoices.





# Money Unexpected Sources

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*They will share more information in a free interactive workshop in July. New Business Minnesota will hold its monthly Startup Meetup networking event immediately following the workshop. For more information and to register and RSVP go to: [www.newstartupmeetup.com](http://www.newstartupmeetup.com)*



# Get Paid for Outstanding Invoices to Keep Cash Flowing

Factoring Companies Lend Money and Offer Credit Management Services In Times of Need.



Rochelle Hilson, Kristin Erickson, North Mill Capital.

By **Kristin Erickson**  
*North Mill Capital*

As your business grows, there will be times when you need capital to build inventory, buy equipment or pay your suppliers. And you may find that a willing bank is not to be found.

At moments like that you need to know your financing options. One solution that many new and growing business owners should know about is called factoring.

Factoring is a financing tool based on the purchase of accounts receivable – invoices. It is essentially the same as a loan.

Here is how it works.

- Factoring companies like us, North Mill Capital (NMC), will buy the receivables at a mutually agreed upon advance rate.
- NMC lends up to 85 percent of the receivables value upfront.
- When the invoice is paid by our client's customer, NMC gets paid for what was already loaned out. The balance is then returned to our client, less our fee.

North Mill Capital's role is to provide a funding source to bridge

the period of time until the business can obtain bank financing. And because we aren't regulated, we can provide the borrower with flexibility that a bank can't. Often, our clients choose to stay with us when they could otherwise leave.

Lenders, like banks, look for cash flow and profits to guide their decisions. They analyze the historic performance of the borrower to determine if they can lend money today. In other words, if you are a new business with only limited history or you launch a new service or product that has yet to establish a track record, you may not fit the bank's lending criteria.

Our approach is different. NMC looks at the collateral already in place, such as receivables, inventory and equipment. Then we evaluate our client's prospective outlook and determine how comfortable we are with future performance.

New businesses or those that are growing faster than their cash flow and bank can accommodate are the most in need of factoring services.

Borrowing through a factoring relationship ensures that the debt remains within a healthy balance with assets so it is hard to overburden a company.

NMC often works with banks where we share the financing

## North Mill Capital *Continued from Previous Page*

arrangement. The client can continue with factoring or return to full bank financing whenever the bank and the client are ready. It can be a short-term or long-term relationship.

Factoring services are a good alternative in either a strong or a weak economy. Companies who might otherwise be unable to obtain sufficient bank credit can rely on factoring as an alternative during that time frame.

Factoring has been around for centuries, and is a great financing tool regardless of the market.

### Case Study

We have a client who manufactures high-end planters for fruits and vegetables. Their growth rate was rapid, and further complicated due to the seasonality of their business. Our factoring solution provided them with more than sufficient credit availability.

We also provided a short-term inventory loan so they could get through their season and deliver to their large retail customers without creating a lot of debt.

Just as important, they didn't have to raise equity – sell off part of the business to investors. They got their money and continued to own 100 percent of their business.

Industries typically utilizing factoring include manufacturing companies, service providers (staffing companies, security guard services, etc.) and wholesale distributors.

Some borrowers are in a start-up phase and some have been in business for more than 50 years.

Most clients are referred to us by a bank, accountant or lawyer who recognize an alternative source of funding is needed. The borrower often doesn't know anything about factoring, just that they have a need for operating capital.

### Factoring Misconceptions

While some businesses turn to factoring because they are experiencing financial challenges, more businesses turn to it because they are experiencing significant growth.

Another misconception about factoring is that the client's customers have to pay the factor directly. NMC operates seamlessly with our clients and their customers are not usually aware of the financing arrangement.

Some business owners mistakenly assume that factoring is too expensive. It is more expensive than borrowing from a bank, but it's less expensive than equity. Factoring is often a short-term tool that is used until you can build a track record that will qualify for a bank line of credit.

### Online Lending

If you have a financing need, there is a good chance you'll turn to Google, where you'll find all kinds of options that appear to solve your problem. The latest financing trend is peer-to-peer or fintech (financial technology) financing online.

It may be a quick and easy source of money, but they have no real knowledge about you or your business and there is no personal relationship. Your information is plugged into a credit scoring model and you qualify or you don't. It can be difficult to

understand their pricing and it can be prohibitively expensive.

You are much better off working with a local lender that can help you work on a comprehensive solution. NMC has a full-service office that has an extraordinary amount of experience and significant capital resources.

We believe being local is a big plus for our clients. NMC wants to be a lending partner with a relationship manager who knows and understands our client's business.

Building that relationship begins at the first meeting with a prospective borrower where we learn about our prospect's business and financial needs to see if it's a good fit. We then evaluate the financial statements and aging reports for receivables and payables. If it makes sense for us and the borrower, we prepare a proposal.

How much we are offering to lend is explained in detail in the proposal. If it is accepted, we move on to due diligence and underwriting and then close the transaction.

It can all come together as quickly as a week, or it can take much longer depending on a number of factors. The better prepared the client is, the faster it goes.

If a client has a need that is outside our parameters, we might be able to work around that or we can refer them to the right solution. We think it's important to surround yourself with successful professionals like good banking and accounting partners. Our clients see us in that mix.

We can also help our client's manage their accounts receivable process, monitor their customer's credit on an ongoing basis, make collection calls if needed and generally help manage their receivables portfolio.

### Conclusion

We can't stress enough how important a good business relationship is. A client may come to us at first thinking they just need financing, but as we work with them, they realize NMC can help them in other parts of their business.

What makes this business fun for us is seeing a company that is struggling to get credit, and we are the ones who can make it work. Our success stories are extremely gratifying.

### NBM

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*www.northmillcapital.com*

### Call To Action

To learn more about factoring and see if it is right for your company, call Kristin at (952) 259-6222.

# Looking for Money? Try Sensible Credit Policies

## Selling to Customers with Poor Credit Is Like Throwing Money Away.



By Pam Krank

*The Credit Department*

Many small business owners are so focused on revenue that when they find themselves running out of money, they start making plans to get a loan until they can get sales back on track. The sad truth is that the unfettered pursuit of sales can lead to an increase in bad debt.

Making a sale to a company that has a poor payment history and a bad credit rating is not something to celebrate. Sure you made your goal for the month, but the reality is you may never see some of that revenue.

If you are looking for another source of revenue, just check out the trail of dollars you left behind while taking your leaking bucket of cash to the bank. Stop the leaking with sound credit policies and it will feel like you have a new source of income.

For those of you who sell your products or services on cash or credit card terms, you're already maxing out cash flow from your sales. For those of us who must bill customers and thus extend credit, it's more complicated.

Unfortunately, you can't trust every customer to pay you what's billed, even if they have a long history in business. Today, more than 9 percent of companies worldwide are at high risk of defaulting on their debt. One wrong credit decision could wipe out your profit for the year.

For some businesses that depend heavily on a few key customers, one default will put you in default. With the right steps in place, you can ensure prompt payment on

every customer invoice.

Here are a few steps that can help you manage your receivables and improve your cash flow:

**Step No. 1: Get a signed contract.** Contracts are essential when selling on credit. Contracts outline the terms and conditions of sale and the obligations/limitations of both parties.

If you offer credit and there are no signed contracts, you need the customers to apply for credit. This credit application, called a "Customer Profile" (more customer-friendly term), provides billing information as well as ownership background and important legal protections.

Questions to ask include: How long have they been in business? Who owns the company? Who's the payables contact? What are their sales? Who do they bank with?

In addition, you need them to sign and agree to your terms of sale including late fees, your local jurisdiction (i.e. Hennepin County) in the event of payment default, and an authorization to perform a credit check. These simple, one-page applications will greatly increase your odds of getting paid.

**Step No. 2: Check them out.** If your customer is a public entity, that's easy. Go to Yahoo Finance and research the last four trailing quarters – specifically Cash Flow Statements and Balance Sheets.

If the "Cash flow from Operations" is negative, see how fast their cash on the Balance Sheet will last. Cash terms may be appropriate in this case. Give extra attention to those customers with share prices under \$5.

Scrutinize their financials to see if there's an immediate risk of default. If the customer is private, use your application to check public records to see if they have tax liens, bankruptcies, or vendor judgments against them.



## The Credit Department *Continued from Previous Page*

If they have material filings, odds are you won't be paid. We use [www.accurint.com](http://www.accurint.com) for this service, but there are other sites online that offer inexpensive searches.

For larger risks, get an Experian or Dun & Bradstreet credit report to see how they're paying creditors. Most importantly, contact the bank listed on the application to see how their cash is flowing. If they want a \$10,000 credit line and they only have \$1,000 in their checking account, the odds of getting paid in 30 days are small.

Step No. 3: Bill often with short terms. There's no need to wait until month-end to invoice the customer. When you ship, bill it. If you're providing a service, bill when your payroll hits to keep your cash flowing. My company's terms are "due upon receipt," and we bill every two weeks.

No service terms should be beyond 15 days. You've already given them the service, so they shouldn't be waiting for anything before paying. If your standard is Net 30 because your customers use your product to make something, stick to the 30 days. Don't let your customers stretch to 60 or 90 days. If they insist on extended terms, first have them apply for extended terms so you can check their credit and then try to build that into your price to offset your borrowing costs.

Step No. 4: Follow-up, follow-up, follow-up. Set the expectation early in the relationship that you need to be paid on time. If you wait 60 days to call your customers for payment, you're really billing "Net 60." Customers will use your money for as long as you let them. You need to call on day 31 or 35 if you don't have payment. The squeaky wheel gets the grease, and you want to be paid first.

Don't apologize for wanting your money. Call their payables person and state clearly, "I'm calling on Invoice XXX that was due on XXXX." That's it.

Don't help them not pay you by feeding them excuses. Just wait for them to respond and hold them accountable. You provided your products and services without dispute, so they need to complete the contract and pay. Keep following up if you don't

get paid within a few days – keep calling until you get paid.

Try to have someone other than the salesperson making the collection calls – preferably just one person in the company. If you are the sales person AND the collector, just tell them your bank requires you to collect your receivables within terms.

Step No. 5: If you don't get paid, go after them. First, send out a 10-day demand letter. If they don't respond, start the paperwork to get a judgment against the customer in your county courthouse if they signed your profile.

In Minnesota, you can get a judgment for up to \$7,500 without an attorney. Just watch an episode of Judge Judy for practice...that's small claims court. If you don't have a signed contract with your jurisdiction, you need to go to their county to get a judgment. If the dollar amount is too high, get a third party to help you.

We use collection attorneys and agencies who work on commission only...usually they receive 15 percent to 30 percent of total monies collected. We never pay hourly for third party collection work...the only fees might be a few hundred dollars for court filings.

If you follow these guidelines and create a consistently enforced policy when you're a small company, you will have a much easier time growing your business. Your cash will grow with your sales, you'll reduce your borrowing costs, and your customers will know what to expect in your relationship. Essentially, you'll get paid on time, every time, from your customers.

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## Look for the Startup-Friendly Seal of Approval

These are the businesses that want to work with new businesses.

# Equipment Leasing Can Preserve Your Working Capital

## Don't Borrow Money From a Bank Without Considering the Alternatives

By Lesley Farmer  
KLC Financial Inc.

**Y**ou have a great idea for a business that you know is a winner. For years you've dreamed of the day you can open up your own business and bring your product to the people. You know they'll love it and you're sure it will be a success.

You've done everything you're supposed to; researched the demographics; put together a business plan; determined the equipment, furniture, and decoration expenses. You know exactly how much you have to make to ensure you do more than break even.

Now it's time to put your plan into action and head to the bank to get the loan to get your business off the ground.

Unfortunately, business is full of unexpected turns. What you thought was a simple loan application process ran into a finance reality: Banks have constraints that don't always make sense to individuals who are looking for startup business loans.

That's where financing and leasing companies like KLC Financial come in with customized financing solutions.

### Bouncing Back

A business I recently worked with fit the above description. They had a great plan for a family entertainment center and felt confident when they approached their bank.

Like I said, banks have constraints, especially when it comes to balancing risk. The financing plan called for them to pledge all their assets, plus put down 30 percent to get the loan. They weren't expecting that.

Considering they had already paid the franchise fee, they were getting worried. They were terrified of the commitment the bank was asking for.

Like many banks, this one made the

best deal they could, but their hands were tied. They referred them to me, knowing KLC has alternative financing capabilities.

After reviewing all their options, I was able to put a package together that would finance all the equipment for the facility, using the equipment alone as the collateral.

They were thrilled to preserve their capital, which was needed for other parts of the business. I was able to move fast and keep their launch schedule.

### Leasing Solutions

What that company went through, the path they took looking for money, isn't that unusual. Most people don't know that there are alternatives to solving their money problems.

The first idea in their heads is that they have to purchase equipment, furniture, fixtures, point-of-sale (POS) machines and other items necessary in order to get their business off the ground.

The upfront cost of purchasing is often prohibitive and many times financing the purchase doesn't give a return on your investment that makes sense. Leasing has many advantages and frequently allows you to save some of your capital so you can purchase equipment down the road.

Because KLC Financial is one of the leading leasing companies, we have relationships with vendors and banks across the country. We get referrals from them when they aren't able to find a solution.



## KLC Financial *Continued from Previous Page*

### Evaluating Options

Every business owner's situation is different and it's important that I meet face-to-face with clients and evaluate their business plan.

After that, I'm able to work the numbers to provide a cost benefit analysis, weighing tax breaks, interest rates for purchasing, depreciation and leasing costs. Such a plan will show the benefits of leasing certain equipment to preserve capital now so it can be used down the road to make payroll and other important working capital needs.

Many business owners I meet, think interest cost is the primary consideration when deciding whether to lease, finance or purchase equipment. They'll do a simple analysis that only looks at the loan interest rate and the effective interest rate in making their decision.

What they don't do is a working capital analysis. That is far more important to the business owner's profits than the interest cost. To thoroughly answer this question, one must justify the acquisition by calculating the operating profit the acquisition will generate and then determine the cost of acquisition.

Then they have to objectively consider two perspectives:

**First:** What is the total cost of making the acquisition? The normal rule: the lower the interest cost, the higher the net profits.

Many decision makers fall into the trap of believing this is the only rule and look no further. It can be a good rule, as long as the effect on the amount of their working capital is equal.

This brings us back to the first rule of business: Working Capital is the most valuable tangible asset of a business and must always be preserved for its best and highest use.

The use of working capital creates profit. Leasing allows for the best use of the most working capital, which translates directly to more profit. Leasing means lower cash outlay and effective reduction of tax liability.

Leasing provides ease of maintaining the most effective means of production and also preserves and creates working capital better than any other method of obtaining equipment.

**Second:** Business owners should consider the effect on their personal assets and liabilities. Prudent business owners must know this, or they might be forced to close their doors without knowing exactly what effect that would have on them personally. Have they honored all their obligations? Will their personal credit and business reputation suffer?

If the company can pay cash for the proposed asset, they have added an asset with no liability. A very safe position, but as the old saying goes, "A ship is safe in port, but ships are not built for that."

### Call To Action

If you are looking for financial solutions for your business, either as you launch or to expand, please call Lesley Farmer for free review your financing plans to see if there are alternatives that will better serve your business.  
(952) 224-2901

A capital asset should be acquired with financing or leasing while keeping sufficient liquid assets available to pay off any obligations created in the acquisition, keeping in mind the worst case liquidation value of the asset.

KLC Financial specializes in helping businesses conserve their working capital and improve their cash flow by structuring leasing and financing terms tailored specifically to their needs. We don't take a cookie cutter approach but design each agreement to help our customers succeed – because our success is based on theirs.

Our programs often prove to be a smarter approach than buying or financing because they help businesses avoid tying up cash or credit in equipment that depreciates and becomes obsolete.

We can even provide comprehensive solutions that bundle equipment, software, installation, training and other services into a single convenient lease payment that is often lower than loan payments for equipment alone.

The benefits we look out for are conserving capital for unforeseen expenses, improving cash flow, preserving business and personal credit, avoiding obsolescence by regularly upgrading equipment, bundling equipment, software, installation, training, maintenance and other services into a single lease.

### Small Business Financing

If you're a small business, you know how important it is to maintain your equipment and to pay attention to advances in your industry equipment that can keep your costs down. Whether it's an energy-saving advance, something that makes your business more efficient or even software that can allow you to expand your business or offer a new product, you have to stay on top of it or your competitors can pass you by.

Unfortunately, you also know that all of this costs money. Though you're doing well, and your capital budget is in pretty good shape, once you investigate the cost of this new equipment, you work the numbers and aren't sure if you can afford the expenditure right now.

So you start looking into a business loan, again work the numbers and though the payments are affordable, you don't think there will be a sufficient cost benefit to justify the expense.

### Conclusion

Working with financing professionals like KLC Financial will introduce you to a new world of financing possibilities. This isn't our first rodeo. We've probably encountered your challenge many times before and helped produce a positive result.

It's a smart strategy to understand all your alternatives. When you hear a No, you really need to know where you can find a Yes.

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