

WHAT IS BUSINESS CREDIT?

Why Do I Need Credit?

Establishing a good credit rating is an important financial priority for every business. Having good business credit means that owners of businesses can seek alternative financing for essential needs without having to extend their personal credit.

At some point in every business, owners will require financing. Some businesses require working capital loans. Some need to establish financing in order to build their businesses by financing their accounts receivables, restocking inventory, or investing in much needed capital equipment. Others may want to save money by taking advantage of trade discounts or purchase office supplies in bulk. And unfortunately, the reality is that many businesses find themselves in situations where they need to utilize financing to make emergency repairs or pay for outstanding taxes and assessments.

Today there are a wide variety of loans and lines of credit that business owners can qualify for. For example,

Wide Variety of Financing Opportunities

Lines of Credit: These types of funds offer fast and flexible financing options to meet the short-term cash requirements many businesses cannot survive without.

Long-Term Loans: These types of loans are an excellent source of funding for acquiring higher-cost items, such as office equipment or commercial vehicles. They can also be used to finance leasehold or capital improvements to improve the physical presence of a business. Many businesses utilize these types of funds to finance long-term growth, such as the development and implementation of new product lines.

Short-term Loans: While usually offered at slightly higher interest rates than Long-Term Loans, these funding sources can be a perfect funding source to assist businesses in paying for specific short-term needs, for example, financing the operating costs of a single large contract.

Unsecured Business Credit Cards: These revolving accounts are accepted everywhere personal credit cards are and provide excellent funding source for businesses which need to finance a variety of day-to-day operating expenses, smaller seasonal purchases, and simple business property improvements.

Secured Business Credit Cards: This relatively new business funding option is an excellent source of financial assistance for new business owners attempting to establish a credit record. In order to get a secured business credit card, business owners establish an account with the financing company and use that collateral to establish a revolving credit card account that, after time and positive payment history, can be converted into an unsecured line of credit.

Separating Personal and Business Consumer Profiles

Businesses that have a good credit history are typically eligible for business credit. In order to receive this kind of credit, it is helpful to understand the criteria a lender looks for in a potential borrower. The more closely a business follows these guidelines, the more likely it is to get a credit request approved.

HOW TO GET BUSINESS CREDIT

The Five C's Of Credit

Any financial institution willing to extend credit to a business wants to be confident that the loan will be repaid.

In order to develop a profile for an applicant, lenders typically consider the "Five C's of Credit." This criteria assists lenders in developing an applicant's profile which, in turn, helps them to determine whether or not credit will be extended to the applicant.

Character: This kind of analysis helps a lender to determine what kind of borrower a business will be. Since many businesses who apply for credit do not have a business credit history, a lender's best indication of future business credit character is the personal credit history of the primary individual(s) involved in the business. For instance, a lender may check to see how well a business owner has managed his or her past personal debt. They will consider issues such as whether or not all credit cards have been paid on time, if mortgage payments are current, if there are any outstanding tax liens, and if there has been any kind of bankruptcy in the past 10 years.

Not only may lenders ask questions about your personal credit, they may apply a "Fair Isaac" score that weighs a variety of factors, including length at current address, type of employment or profession, and debt-to-income ratio. The "Fair Isaac" score also takes into consideration the total amount of extended credit, current debt levels, and length of time credit lines have been established.

Credit: When analyzing a person's credit, business credit lenders will want to know that your bills to suppliers and other vendors have been paid consistently, as well as if payments to other financial institutions are current.

A potential lender can verify all of this information with a credit-reporting agency such as Dun & Bradstreet. Agencies such as this issue business credit reports which include all reported information about outstanding loans, current credit limits, property taxes, and even child support payments which they acquire from the agencies

and financial institutions that have lent you money or extended you credit.

It is highly recommended that you get a copy of both your personal and business credit reports and regularly review them to verify that the information included in them is accurate. Any time you are denied credit, you are entitled to a copy of your credit report from any one of the three major reporting agencies, including Trans Union, Experiean (TRW), and Equifax.

Cash Flow: Lenders also want to have a sense of how consistent and predictable your cash flow is. Most financial institutions that extend business credit are cash flow lenders which base their decision to lend you funds on the cash flow that you generate and ultimately use to repay them.

In order to compute a businesses cash flow, simply combine a company's net profits plus its non-cash expenses (amortization and depreciation). A reliable guideline is that for every dollar in combined loan payments, a business should be able to generate a cash flow of \$1.50.

Capacity: A business's capacity to repay any loan or extended credit in the case of an unexpected economic decline is considered its capacity. In this case, the lender wants to be assured that the business has the ability to convert existing assets to cash.

For instance, lenders must feel confident that, in a worst case scenario, the business could acquire additional financing by selling real estate holdings, stocks, or CDs. The potential to cash in savings in order to meet payment obligations is also a critical factor in acquiring business credit.

In order to verify a business's capacity, potential lenders typically ask for a business balance sheet, recent state and federal tax returns, as well as copies of several months' financial statements.

Collateral: In order to feel safe issuing a secured loan, a potential lender will verify assets that could potentially be used for repayment, such as business assets (including accounts receivables, inventory, equipment, or real estate) or even personal assets (checking or

savings accounts) or even personal assets (including financial investments such as stocks, bonds, or CDs).

In the case of an unsecured loan, a potential lender will not take into consideration collateral. Instead, it will rely on the strength of the business's character, credit, cash flow, and capacity.

Obstacles to Establishing Business Credit

Two of the most common reasons why business credit is difficult to establish have to do with having no personal credit history or the length of time a business has been established.

Business experience, personal references, and work history can sometimes be substituted for this type of history. But there are a variety of other ways to build your credit standing.

Pay All Bills on Time: This is an excellent way to establish a positive personal credit history. After you open a checking account, you need to make sure you pay all your bills -- rent, phone, electric, medical – on time every month. These on-time payments will be reported to your credit record and will help to demonstrate to prospective business lenders that you have the discipline and willingness to pay your obligations – as well as any future debts.

Qualify for a Loan with a Co-Signer: Another way to establish a positive credit history is to apply for a loan with the help of a relative or friend with excellent credit. By co-signing for your loan, your friend lets you borrow you his or her good credit standing to qualify for the loan and promises to repay the loan if you default.

After using the credit account responsibly for one year, you can reapproach the lender and apply for a loan or credit card on your own.

Secured Credit Cards: Applying for a secured business credit card is another way to establish a positive credit history. A secured business credit card is different from a non-secured card because it is guaranteed by funds you deposit in a collateral account.

After keeping a good credit standing and making on-time payments for a period of time, a lender may consider switching the credit card to either a partially-secured product (refunding a portion of the collateral deposit) or to an unsecured business card (refunding the total amount of the collateral deposit).

Building Credit With Secured Card

For small businesses, access to credit is vital. Some financial institutions now offer secured business credit cards. These cards are especially suited for business owners who need to build their business' credit profile.

Some accounts may allow YOU to earn interest on the collateral account, which is used to secure the credit card spending limit.

You can use a secured business credit card for all types of business expenses. And this type of credit card can benefit your business in other ways as well.

- * By giving you access to additional funding, the credit available on this card may serve as a valuable cash flow tool for your business.
- * If you are a business owner that relies on personal credit to help run the business, a secured business credit card will enable you to increase the amount of credit available.
- * It helps you build your company's credit, which enables your business to compete for government contracts.
- * Cards can be issued to your employees to make it easier for them to make business purchases and to help your business track their expenses.
- * You'll receive monthly statements and quarterly reports detailing all charges, which will simplify your record keeping.
- * You can use it to keep your personal expenses separate from your business expenses. Banks are in the business of lending money to businesses that need money. If you need business credit -- for a specific purpose, for ongoing expenses or for expansion -- work with

your business banker to find the loan, line of credit or credit card that will help you achieve your goals.

Companies Incorporated is a national leader in corporate and business credit services. We offer several levels of service to build a separate business credit profile. Please visit our business and corporate credit section to learn more:

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