Can I get a loan to support my business?

DECAL
Thriving Child Care
Business Academy

Accessing capital is an important component of managing business finances, especially for small businesses. Use this resource to learn how and when to access capital and strengthen your business.

Business debt can be a blessing or a curse. On the one hand, it can help you grow your business and realize greater profits. It can also create efficiencies to make your business even more profitable and resilient in the future. On the other hand, business debt also comes with risks. It can provide additional costs for your business long into the future that could make growth difficult or even impossible. Accordingly, when considering taking on business debt, it is important to consider why you need it and develop a plan on how you will pursue it, use it, and pay it back.

In this guide, we are going to take you through some of the questions you might want to ask before seeking business debt as well as the different types of loans you could pursue. Finally, we will go over some questions you might want to ask when selecting a lender.

Good Debt vs. Bad Debt

Debt can help or hinder your business's success. To tell the difference between "good" debt and "bad" debt, you can assess the level of risk involved as well as the likelihood of success.

Good debt is generally any sort of debt that has a **high likelihood** of leading to increased future revenue and/or profitability. Profitability is how much money you have left after paying all your expenses. This kind of debt is likely to offer a strong return on investment and help sustain your business resiliency into the future. As such, this makes the accumulation of debt for these purposes a **lower risk** than other types of debt.

For example, pretend you are a family child care provider and you have been in business for years. You have a great reputation and have a strong and loyal parent following. You have a long waitlist and several families asking you to expand your services, but you have already reached your capacity. You do know of a potentially viable location for a small center right in your neighborhood into which you could expand. Expanding your in-demand service to families in your area will enable you to increase revenue and profit for your business. In this case, the debt to expand your business can help scale your business growth.

Bad debt, in contrast, is generally debt that is **unlikely** to lead to increased revenue or profitability because you are uncertain of the outcome of the investment. As such, this type of debt is considered a **higher risk** since you might or might not see a return on this investment.

For example, at the height of the pandemic, some child care businesses under great economic stress took out loans just to survive a few more weeks. The investment was taken on to keep afloat because they were committed to serving their families and communities. However, often there was no long-term plan to increase revenue or profit or to repay the loan. In this instance, you might be able to extend the life of your business in the short term by taking out a loan, but without a clear plan to increase needed profit and repay your debt, the loan will likely leave your business in a weaker financial position than when you started.

Unethical debt refers to business debt that is taken on for improper reasons. For example, if a business owner took on debt because they believed they could receive funds with a lower interest rate than through a personal line of credit, but they do not intend to use those funds for business purposes, this would be an inappropriate use of a business loan. In addition to causing a messy financial situation, the business now has the added stress of paying for a loan that doesn't increase the business's revenue or profitability. In a case like this, the additional economic stress on the business can lead to difficulties, if not closure, and the decision could bring with it potential legal troubles or bankruptcy.

Questions to Consider

Regardless of the type of debt that you take on, it is important to thoroughly consider the pros and cons before jumping in. In addition, having a sound budget in place can help track business health over time to recognize and respond to trends in advance. Taking on business debt is a big decision, so it is critical to think through everything beforehand, including your plan for repayment. To help you with this process, take a moment to answer the following questions. Such major decisions warrant taking time to consider your situation to ensure that you have clarity before you move forward. Take some time to put your thoughts on paper and review your answers before you act.

What am I going to do with the money? At the most basic level, you will want to start by understanding if these funds will fulfill a short- or long-term need and as such, whether repayment will be short- or long-term. For example, a short-term loan might be used if you want to renovate your existing program to add one more classroom. You need the lump sum payment upfront but have a plan to repay the debt within one year. A long-term loan might be for a larger project, such as taking on debt to invest in transitioning from a family child care program to a center located in your community. In this case, the loan would take longer to pay off and would require a plan to build up the base in revenue and profitability to pay off the debt, which will take some time. As you can see, the decision to take on debt and your plan to pay it off is driven by your vision for your business. It is important to clearly outline what you plan to do and why you are doing it to ensure that you have a solid plan for a repayment timeline.

Are families willing to pay for it? When you think about this business growth, it's not enough to just think about what you want. You must also consider what you believe the market wants, or in other words, what the families in your community want and need. Consider our previous example in which a family child care provider is interested in transitioning to a center within the community. In this instance, it would not be as simple as saying, "I have a lot of families who are already using my services and others on a wait list" and then moving forward with the loan. You want to ensure that those families would be on board with your decision, or else the investment would not be as profitable as you expected. Do these families wish to move to a center with you, or do they prefer the family care that you already provide? Is the location desirable for them? Do the families on the waitlist feel the same as those already utilizing your services? It is important to write down whether or not you think families are willing to pay for your proposed change as well as the evidence that you have to support that.

How much money do I need? Now that you have your vision written down, you can start to get an idea of how much money you need. This is not always as simple an answer as it seems on the surface. We recommend breaking out your costs into two general categories: 1) How much startup money do you need? and 2) What's the long-term funding you will need?

Let's take the example of the family child care provider who's moving into a center. In terms of **startup funding**, the provider may need to pay the first and last month's rent on their new facility. They might need some money set aside to help renovate it before the center can open. Or they might need to pay staff for onboarding and training before an official opening. Further, during the first few months, the owner may need to invest in additional resources like an accounting system or child care management system. It is wise to budget for those resources and to write them down individually.

In terms of **longer-term costs**, the reality is that no business expansion is realized overnight, and long-term costs should be expected. As such, our example provider might wish to estimate the first six months of operation costs and factor those costs and anticipated revenue into the funding request. The provider should ask themselves, “If I had to be ready to open my new center tomorrow, what would I need?” They should also be certain that there will be adequate funds to keep the business running smoothly long enough to see the anticipated increase in profits.

Combined, you will want a safety net of funds that will ensure that you are successful in your endeavor and will not have to stop scaling before your growth is fully realized.

How is my credit? When thinking about applying for a loan, you will need to consider the credit that your business might have as well as your personal credit. It is wise to be aware of measures of credit strength and go into conversations to discuss a loan with open eyes. Even if your business has been around for several years, if your business hasn't taken on a business credit card or other loans in the past, you might not have a strong business credit history. Just like personal credit, banks can be leery of requests which are not backed by

strong credit history because they cannot be sure that you can handle the credit.

Additionally, many business loans will require you to secure the loan with your own personal assets and money. That means that your personal credit score may also come into play. If you worry that your credit history and score are not as strong as you would like, this does not mean that you should give up hope. As you pursue your loan, let the partners you're working with, whether it's a Small Business Development Center professional, a bank, or a financial technology company, understand where you think your credit lies and why. This will help them assess which loans may be the best fit.

Will I be able to repay the loan? While there are clearly good types of debt that have lower risk and a higher likelihood of financial gain, keep in mind that any type of debt that you take on will become bad debt without a solid and certain plan to repay it. You will need to consider what the monthly payments will be and make sure that you can handle the financial burden until your debt is paid in full. In most cases, you will want to calculate how much extra money you will need each month to pay off the borrowed amount (plus interest) over a given period while still paying your regular business expenses. Determine where the money will come from and what you will need to pay each month or over the course of a year to have your debt fully paid by the end of your loan term (or the desired amount of time). An online loan payoff calculator can help you make sure that you have a solid plan to repay your debt in a timely manner to avoid any costly repercussions for your business.

Types of loans

Once you have a sense of whether or not you want a loan, how much money you will need, and how much existing debt you already have, you are going to want to consider the funding streams that are available to you. There are many types of loans, but this section covers the ones that are most commonly used to support center-based and family child care businesses.

Friends and family

One of the great misconceptions around business debt is that it works just like you see on TV: somebody has a great idea for their business, they go to the bank, the bank gives them a big loan, they expand their business, and everyone lives happily ever after. When you look statistically at the way businesses gain the credit to grow, overwhelmingly the source of funding is friends and family.

Friends and family already know who you are and may be more likely to buy into your vision for your business growth. Connecting with family for help may be as simple as asking your parents for a loan or for a contribution to get you started. Another option for reaching out to friends and family who believe in your business vision could also be crowdsourcing. As we've seen on sites like Kickstarter or GoFundMe, you, as the business owner, can present your plan and funding goal to others to ask for help. Often, friends, family, and even people you do not know can rally to support your cause. In many cases, your friends and family might not be able to support funding your business dreams, but it is

always worth taking a moment to evaluate the people who know you as possible sources of support.

For example, one center that recently needed to revamp its playground equipment could have applied for a business loan or used a business credit card to fund the investment. Instead, they started a GoFundMe campaign. Through friends, family, and community support, they were able to raise the money needed. This center, located in an under-resourced neighborhood, was able to reach friends, family, acquaintances, friends of friends, and so on. Their extended social network was able to come together to support the center's effort to provide high-quality equipment for the children at the facility.

When you secure funding through friends and family, we recommend that you treat the agreement just like any other loan you might pursue. What this means is that you will want to ensure that you put your agreement in writing and avoid the temptation to say, "We shook hands on the deal; we're good to go."

Your agreement doesn't have to be a 40-page contract, but it should include some items that clarify key details of the loan. These points should include how much money you owe, whether it is only the borrowed money you owe them, and if you also will owe them a percentage of the profits of the business in perpetuity. You will want to include in your written agreement the amount of each payment that will be made on the loan, the interest rate, and what portion of each loan payment is principal (the original borrowed amount) versus interest (a percentage on top of the borrowed amount that it costs for you to borrow money).

You will want to make sure that the amount that is due monthly is clearly outlined along with the total number of payments that will be made, the interest rate at which you are borrowing, and if interest will be a flat percentage of the original amount borrowed or a percentage of the remaining balance calculated each month. Consider having an attorney or uninterested third-party review the details.

It is a good idea to have this written agreement signed in front of a notary or some other witness to avoid any future complications, even if it is a close family member. Remember to keep a copy of your agreement to ensure you are following the contract details accordingly with on-time payments in the same manner as you would a bank or any other lender.

Business credit cards

Business credit cards are a simple way to access funds for smaller, short-term, more immediate funding needs. For example, maybe you don't have cash on hand to pay for a repair, but you know you will by the end of the month, so you could use your business credit card. A business credit card lets you start building your credit history as soon as you open the account, which will be helpful if you need larger amounts of funding in the future. The disadvantage of business credit cards is that they are typically offered at a higher interest rate and may not provide access to the amount of money you would need for a larger expansion or project.

Business line of credit

A business line of credit is from banks or other lenders and is another great short-term loan vehicle. It acts similarly to a credit card but works for slightly longer-term purposes. For example, pretend you are expanding your business, and you need to cover two weeks of payroll while new families are brought into your care. In that case, you may want to use a business line of credit.

The advantage of business lines of credit is that they are flexible. At any time after you are approved, you can withdraw funds from the line of credit up to the full amount for which you were approved. You do not need to use the funds immediately, nor do you need to use all of them at once. The other advantage is that you may only take out the amount you need. For example, if you have a business line of credit for $10,000 and you only need $4,000 temporarily, you can take out the $4,000 and only pay interest on that withdrawal until you pay it back. You would still have the remaining $6,000 available to draw upon in times of need.

The downside is that you typically have a much higher interest rate on the amount borrowed because it is short-term debt. As such, business lines of credit are best for short-term or temporary costs to cover immediate needs that can be paid back in a relatively short period of time.

Term loans

Term loans are a very common loan structure. Many mortgage loans are set up in this way. There is a set amount that you are borrowing that must be repaid by the end of the loan term, which means that there is a time when the loan starts and when it has to be completely paid off. There is typically an associated interest rate that may be fixed or may be variable, that is, it may change over time. These types of loans are usually best for a very specific project or activity in which you know how much it is going to cost overall and you have a sense of how it will fit into your day-to-day business. Most importantly, you know exactly how long you have to repay the debt.

Your loan term could be 5 years, 10 years, 15 years, or 30 years depending on its size and type. The interest rate varies based on your circumstances and the current economy. Term loans might be a good option for expanding your playground if you know that you can pay it off within five years or even for purchasing a commercial property and paying it off over 20 years.

Term loans are longer-term debt, which, of course, could put some strain on your business. The advantage is you typically know what the recurring payments are going to be and can figure them into your long-term budget.

US Small Business Administration Loans

One of the most popular ways to get the business debt that is needed to expand any small business in America is through US Small Business Administration (SBA) Loans. These loans are typically lower cost and lower interest than a term loan you might get from a bank because the government backs, or sponsors, the loan. However, the small business

loans discussed in this section are ones that the SBA backs and supports but are lent by commercial banks that have been approved to do this kind of lending.

- SBA 7(a) Loan
  The most common and popular SBA program is the 7(a) loan, which provides loans of up to $5 million. The 7(a) loan can be used for working capital to keep your business going as well as expenses like real estate, equipment, and other purchases that you make to expand your business. Usually, the interest rates are somewhat low, and the repayment periods are longer term (10 to 15 years). One challenge to getting a 7(a) loan is that they typically go to businesses that have some established business credit history. If you need a loan, the SBA 7(a) loan is still worth talking about with your lender even if you have concerns about your credit history; but it is worth being aware that this could impact your ability to qualify.

- SBA 504 Loans
  The 504 loans are typically used to acquire or expand real estate. If you are looking to go out and purchase a new facility, including a center and the land, or you need to renovate a large playground, this might be a good loan option for you. The 504 loan usually requires you to show that at least 10% of the down payment is going to come from your own business funds. The rest of the money can come from community-based lenders and other traditional banks supporting it.

- Microloans
  Finally, microloans are small loans from the SBA for up to $50,000. Usually, these will come from community development institutions, not from commercial banks. The average amount of a microloan is $14,000.

  Microloans are useful for shorter-term projects which don't require a whole lot of money, but the cost is larger than the limit on your business credit card. Microloans are often a good option for businesses that don't have much of a credit history because they are less difficult to get than other loans, such as the 7(a) loan.

Questions you should ask your lender

Often when a child care business owner goes to get a loan, the meeting can very much feel like an interview focused entirely on the owner. You will likely be asked questions about your credit history, business, and vision. This can create the illusion that everything is up to the lender to decide. However, remember that you also have the right to make sure that the lender is a good fit for your business. It is imperative to ask your lender questions to ensure that your specific needs are met. The right loan can tremendously help your business whereas the wrong loan can damage or even end it.

Does this lender understand child care? Does this bank truly understand your business, both where it is right now and the directions it can take in the future? Is this lender only used to working with other types of businesses in dissimilar industries? Maybe they

typically lend to factories in the area and therefore they might not be able to understand your specific needs.

Is the debt too short or too long? If a loan needs to be paid off too quickly, it could lead to bigger payments that can swamp your business. If the loan needs to be repaid over a long period of time, you could face higher amounts paid in interest on the loan. If the loan is for a long duration, you will want to ask if you can pay the loan off early without penalty since paying off debt early can save you thousands of dollars in interest.

What is the total cost of the loan, principal, and interest? Interest rates add up. Sometimes we look at the amount borrowed and at first glance and assume the monthly payment seems quite manageable. For example, pretend you have a minimum monthly payment of $300 and you feel confident that you can make that payment each month. However, that payment will include the interest due. You could end up with only a small portion of your payment going toward your principal balance and reducing the total amount that you owe. This can result in very large amounts of interest paid over time; and in cases where the loan term is not fixed, it can leave you making payments for longer than you had originally intended. For this reason, it is critical to be aware of your interest rate and the total cost over time as you weigh the pros and cons of your loan options.

When is the first payment due? In some cases, your first loan payment could be due right away. In other cases, only interest may be due for a portion of your loan term and the principal balance may be added to the monthly amount at a later date. Be sure that you are clear on when your first loan payment is due and what it will include so that you can plan accordingly with your business.

How long will the application process take? You will also want to understand what the loan application process involves as well as how long it is expected to take. Ask your lender what forms will need to be filled out, what documents will need to be supplied, and ultimately what the chances are of receiving the loan for which you are applying. You will want to make plans accordingly while you wait for the loan decision to be made. Also, you should be able to weigh whether the time spent on the application will be worth it when you consider the odds of your loan application being approved.

Even after you have answered all these questions, **speak to current and past customers** when you can. Ask the bank for referrals to people and businesses who they have worked with in your area, preferably businesses that are in the child care industry so that you can learn about experiences that are likely most similar to yours. Another way to learn more about potential lenders is to ask your friends and family to see if anyone has received a loan from this bank or institution before and what their experience was like. Understand that this information is absolutely critical to making an informed decision. Ultimately, it is not just the bank's decision; it is your choice, too.

Getting Help

If you are ready to look at specific loans and/or feel you are ready to pursue a loan, you can reach out to your local Small Business Development Center (SBDC). These are organizations sponsored by the government in place to help your business thrive long-term. You can easily find your local Small Business Development Center by going to americassbdc.org/find-your-sbdc and entering your zip code. The local SBDC will come up and you can reach out to them directly.

Additional Resources

If you have questions or need help, assistance is available.

GaPDS Website

DECAL Thriving Child Care Business Academy Website

Georgia Licensing Rules and Regulations

To Find Other Study Guides: Click on Resources on the Academy home page

To Find Training: Click on Trainings on the Academy home page

To Register for Training: Click on Schedules & Registration on the Academy home page

To Sign Up for Study Groups: Fill out the Intake Assessment

For questions about coaching or study groups: Email GAcoaching@civstrat.com

To Find Other ECE Resources: Visit the DECAL Website

For General Questions about the Academy: Email thriving@decal.ga.gov

For More Information:
Family Child Care Learning Home Rules and Regulations

Child Care Learning Center Rules and Regulations

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