Feeding Growth:
A Guide to Financing Expansion of For-profit or Non-profit Business

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This paper addresses types of expansion funding available for organizations, whether for or not for profit,, that have less than 50 employees, and have established a track record through at least one year of successfully providing goods or services.

An organization's growth usually involves expanding market share, providing new goods or services, or providing the same product or service to new markets. Whether a simple service organization, a lifestyle business, or a full-blown business operation that aims to dominate its industry, growth is not an ego-fulfilling exercise; it is an imperative that underlies all ventures. In today's dynamic world, the absence of growth no longer means standing still: Instead, it means shrinking and, sometimes, disappearing.

There are many financing options to consider when you're ready to expand and need money to do it. Some are obvious, and some are more hidden, accessible only to those who conduct intense research. But all options involve one simple equation: you must present your case to a financing source in a way that addresses their interests. Therefore it is important to understand how financing sources think.

Typically, the for-profit and non-profit business worlds are treated separately, but these days the boundaries between the two are getting blurrier in terms of business approach, common terminology, and the things financing sources look for, so in this document we will address them both.

What Every Financing Source Will Want to Know

Financiers are not your enemy. Typically, every type of funder wants to be seen as a partner in your success. Their job is not to "beat" you in the game, but to collaborate so that you are both successful. They expect to create a relationship that will last well past the date when they sign the cheque, and the time and effort you spend on approaching them in a professional way tells them a great deal about what to expect from you once the deal is done.

However, financiers' most common concern is risk and reward, and so they establish systems to measure how much risk the financing will create, and what kind of reward it will generate, not only for themselves, but also, as is often the case with non-profits, for society at large. They do this by establishing a set of criteria for an individual or organization that is invariably based on some combination of **character**, **capacity**, and **collateral**.

In the broadest possible sense, these terms can be defined as

Character – The educational and work background of key staff, past successes of your organization, and the way you make your case for funding. All of these are indicators that tell a funder whether you can be trusted to use their money in the way that you say you will.

Capacity – What is your current size, financial status, and degree of relevant expertise in relation to your planned growth? Are you the right organization to move into the proposed area? Are you in a position to repay the funds if things don't go as planned?

Collateral – What are you bringing to the table that shows your dedication to this project? For a bank, this would mean the assets that will be forfeit if you can't repay the loan. For a grant funder, it is often referred to as **matching funds** and refers to existing assets your organization will use towards the same goal that the funder is supporting. In both cases, the point is to demonstrate that you are serious about this goal, and that you wouldn't ask anyone else to take a risk on your organization unless you are also willing to take a risk on yourself.

Another way to look at it is in terms of a good story. Like all human beings, financiers like to hear a good story that answers the above concerns. So if you're looking for expansion financing, you have to provide them with a compelling story.

Storytelling for Funders

Every successful story should answer six basic questions: who, what, where, when, why and how. Who are you, what do you do, when and where are you going to do it, why are you going to do it, and how are you going to do it? (A crucial point to note here is that for funders why generally does not mean 'why are you doing this?' It means, 'why does your intended audience want this product or service?') A potential funder who looks at your financing proposal should be able to find the answers to these basic questions quickly and easily.

Other questions that are specific to storytelling for funders, and that will require a bit more detail to explain, are these:

How much? – Your financial projections will be subject to change for any number of reasons, and most funders acknowledge this. Still, it is important to demonstrate that you know how to estimate income and expenses for your particular industry, and that your operations will be guided by a fiscal plan. A detailed plan will also help you identify and respond to fiscal challenges while they are still small and manageable.

What is the Return on Investment (ROI)? – This is another chance to show that you have a realistic understanding of your industry. The projected ROI should be appealing, but not over the moon. The amount of time it will take to achieve that level of return should show that you understand the typical speed of change for your market. For non-profit organizations, it is increasingly common to think of positive social outcomes from the project as a form of ROI, and you may want to develop a cost-per-service number that you can present to potential funders (i.e. "send a kid to camp for just $29.50").

Who is the Competition? – There are very few completely unique products or services in today's world. Chances are, you are offering a better version of goods or services that people already use, and you will need to explain how it's better, and how you will make sure that your market understands what is better about it. For non-profit organizations, it is important to address how you will partner with similar organizations to provide improved services where possible. If partnering is not possible, it is important to explain why your services are unique.

Grants, Tax Credits, Investment, or Lending: Which is Right for You?

Types of Funding: An Overview

It's worth looking into all of the financing options available whether you are currently a for-profit or non-profit organization. If the purpose of your expansion fits the funder's goals, then it may be worthwhile to establish a subsidiary with the correct tax status and start a conversation about working together. The following types of funding will be discussed:

Grants
Tax Credits and Rebates
Investment
Lending

Grants

Government grants are typically for projects that relate to social services for underprivileged groups or services for the general public in areas such as education, arts, culture, and scientific research. Grants from private foundations include all of these areas, and some fund religious organizations as well. Economic Development grants are probably the most misunderstood category. These funds are provided by both public and private sources and can be used to create jobs and profits, but the project must have a significant impact on a population with high rates of unemployment or poverty to qualify.

Who Qualifies: The majority of grants are for non-profit organizations. However, grants in the areas of scientific research are more likely to be open to for-profit applicants as well. In some cases, it may be worthwhile for a for-profit to establish a non-profit subsidiary in order to undertake a project with widespread public benefits.

What Type of Projects Qualify: The single most important criteria for receiving a grant is that the project is primarily designed to benefit members of the general public. Grant makers are not interested in how your organization will benefit, but in the results for the audience you are serving with your product. You do not have to provide the resulting goods or services for free, but they must be affordable for the intended audience, and usually any profits must be put towards further serving the same public service goal. Improving the quality of life in your community should be the ultimate goal of a grant-funded project, and the money is just a means to that end.

What Type of Projects Do Not Qualify: It is very rare for grant-makers to cover general operating expenses. The costs must be broken out as costs specific to a new program that will provide new benefits your organization has not been able to offer before.

How to Show That You Qualify: Grant guidelines vary widely in terms of the level of detail they request about your project, but all will touch on the questions discussed under Storytelling for Funders in this report. The majority of grant makers will also provide clear links to their grant guidelines on their web site.

Be Careful About: Although grants are "free money", there are definitely strings attached. Look closely at the evaluation and reporting requirements. Many funders now want the grantee to hire an external evaluator, spending time and money to make sure that the project is going well and that it is achieving the intended goals. This is an important and worthwhile step for larger organizations, but for smaller ones, it can

sometimes be a major drain on resources. Government grants often involve submitting detailed quarterly reports, which can be especially time-consuming for smaller organizations with no administrative staff.

Tax Credits and Rebates:

Tax rebates for activities you may already be doing can often provide larger sums than grants or other investments. Canada offers tax rebates for specific economic areas such as the Scientific Research and Experimental Development (SR&ED) Program, and the Industrial Research Assistance Program (NRC-IRAP). Businesses in the U.S. should review IRS publication 535, available on the IRS website, to make sure that you are taking advantage of all available business deductions. Additional savings in this area can allow you to invest in your own growth, rather than seeking outside funding.

Who Qualifies: All businesses should be maximizing their deductions for business-related expenses, but specific Tax Rebate options may apply for Canadian businesses involved in science, technology, and manufacturing.

What Type of Projects Qualify: Projects that "will lead to new, improved, or technologically advanced products or processes" qualify for the SR & ED program, according to the Canada Revenue Agency. The IRAP program provides a "non-repayable contribution" to projects that are more directly focused on commercializing new technology. IRAP can also provide funds to help cover the salary for recent graduates to serve as interns at your organization if they will be assisting with commercialization-related research.

What Type of Projects Do Not Qualify: For SR & ED: research in the humanities or social sciences; testing or production of a product that has already been designed; development based on "routine engineering practices." For IRAP, it is necessary to contact your regional office for further information.

How to Show That You Qualify: For SR & ED: Specific tax forms will be submitted as part of your annual return, and an accompanying narrative will explain how your project involves a significant contribution to the current body of scientific or technical knowledge in your field. For IRAP it is necessary to contact your regional office for further information on applying to participate in the program.

Investment

Investors will look at your business in terms of the Return on Investment they can expect at some future date, but typically, investors are more patient than banks, and will provide capital you can use to build your business over several years. Because they are taking a position in your business, they also typically want to have some degree of involvement in your business operation. While some investors are passive, most are actively involved in guiding the business.

Investors are primarily concerned with **scale**, or how quickly you can ramp up your business operation to a larger size. If your goal is to double your business over three years, most investors won't be interested; if your story is about growing it by a factor of 10 they'll likely take a look. Investors are also extremely interested in their **exit** from the business: when and how they will cash in their position and move on to another investment. Without an exit strategy in place, no investor will provide financing.

Typically, an organization must follow a **chain of investment** that involves successive levels. Most early investment comes from **love money**: family, friends and acquaintances. Next are **Angel Investors** who participate early in a company's life, when smaller amounts can have a significant impact. **Venture Capitalists** can provide larger amounts, but will not usually take an interest until the company has reached a certain size and established a history of success with smaller investments. **Public investment** involves posting your company on a stock exchange in order to raise funds from retail or institutional investors who

buy your stock.

Who Qualifies: Generally, businesses that have made it through the concept and early development phase, and are actively delivering goods or services.

What Types of Projects Qualify: Projects where the business can make a strong case for an attractive Return on Investment, based on a narrative description of the relevant market, the organization's expertise, and detailed financial projections.

What Types of Projects Do Not Qualify: Nothing is inherently off-limits, but some of the most important factors are an innovative concept with clear market applications, and a team with evident expertise in the field.

How to Show That You Qualify: At a minimum you will need to develop a persuasive Business Plan, but building strong personal relationships is also a crucial part of this process. Most angel investors and venture capitalists have a network of trusted colleagues who vet projects for them, and refer potential investment candidates. You will need to make a positive impression on members of this network before meeting directly with your potential investor.

Be Careful About: Ultimately, the relationship between your organization and any private investors is a very unique and personal one. Many investors see themselves as business mentors who will serve as a coach and, to some extent, as a management partner in your organization. Be sure that both sides are clear on the degree of involvement and control that comes with the initial investment. Be aware that your investor may increase their level of involvement if they perceive a threat to the original plan.

Lending

You might get a loan from a bank, a friend or relative, or one of the newer sources such as private lenders or Internet based peer-to-peer lending. The lender usually expects this money to be returned within 3 to 5 years, and with a fixed rate of interest that is not based on the performance of your business. Leasing some of the equipment you need is another way to create more up-front operating capital and pay off the costs over time.

U.S. (and State) and Canadian (and some Provincial) governments also provide low-interest loans, and loans accompanied by free technical assistance, in areas of specific interest, and these options may be worth investigating before going with a bank loan. In Canada, many of these programs can be explored through the Business Development Bank of Canada, which is owned and operated by the government, or through the Industry Canada website (strategis.gc.ca). In the U.S., low interest loans from the government are treated as being similar to grants, and you can generally find information about them in the same area of each agency's website.

Common Types of Business Loans: The three most common types of loans for small businesses are Unsecured Credit Lines, Short-Term Loans, and Long-Term Loans. An **Unsecured Credit Line** can go up to a set maximum amount, but you borrow only what you need when you need it, which allows you to avoid paying interest on the full principal amount if your needs turn out to be smaller. This works in a similar manner to a credit card, but is preferable to funding your business on your card because the interest rate is much lower. A **Short-Term Loan** will generally be 3 to 5 years and provides operating capital for your business. Some form of collateral will need to be agreed upon to secure the loan. A **Long-Term Loan** is generally for property or some other specific fixed asset, and the asset in question serves as the collateral.

Like a personal mortgage, these loans come with a wide variety of interest rate options and pre-payment penalties, and it is worth shopping around to find the best options for you.

Who Qualifies: The management staff must have a good credit history, or be willing to put up business or personal possessions of sufficient value as collateral. Some lenders will provide loans for receivables, contracts, or other forms of collateral.

What Types of Projects Qualify: Projects that can show a realistic ability to repay the loan. Almost any business can qualify to lease equipment.

What Types of Projects Do Not Qualify: For larger amounts, it is necessary to have both a strong business plan and a strong credit history. Funders will look at the personal credit history of key management staff as well as that of the business.

How to Show That You Qualify: Your business plan should cover all of the points discussed in Storytelling for Funders above but with a strong focus on market and financial information, and less on your product or service. A wide variety of sample business plan formats can be found on the web. If you are looking for financing that is larger than simple personal loans, you may want to find a consulting firm to help you with this part of the process.

Be Careful About: Lending is all about cash flow and ability to repay on a regular basis so, even if you can find lenders to approve them, do not take on too many loans at once. Similarly, do not borrow (or lease) amounts that are so large your cash flow is severely affected. Small operations should only work with fixed interest rate financing, in order to keep costs more predictable.