FINANCING TO FUEL GROWTH, ACQUISITION AND SUCCESSION: WORKING CAPITAL

Obtaining a basic working capital loan could be, ironically, the most important next step you take to facilitating your exit plan or succession plan. This discussion applies as much to prospective buyers as well as to sellers and business builders. This type of loan should be considered the initial point of entry into the bank financing system. If you are in the process of building out or improving your systems and processes, expanding operations, or generally preparing for an acquisition or other means of rapid growth, these loans are an excellent tool.

Unlike a line of credit (LOC), a working capital loan is fully amortized (up to ten years). The underlying idea is that with an amortized payment imbedded in the cash flow, the advisory practice can demonstrate its capacity for regular debt service. This contrasts with paying off a LOC with varying payments depending on whether you had a good or mediocre quarter or year. Although some practice owners counter that they'd simply be happy with a small LOC, don't want a loan or debt on the books, or that they don't really need a full working capital loan, there are solid rationales to reconsider the proper use of debt in your business structure:

1. Prospective buyers often cite the need to grow as the primary reason for acquisition, but it is more important to first grow in terms of both revenue strength and enterprise strength to support a successful and aggressive acquisition strategy in the future. A working capital loan can be used to help grow a practice into a business before ever approaching a seller.
2. If the opportunity to purchase a small book or practice appears, the cash is readily available.
3. There is a famous adage in the banking world – always borrow money when you don't need it.
4. If the preference centers on an internal exit plan or succession plan, a working capital loan demonstrates to next gen advisors that the business is committed to growth by utilizing a working capital facility to drive growth opportunities. (and frequently G2 advisors are hesitant to take on debt. Better to establish that cash flow pattern ahead of time.)
5. This loan format adds a measure of certainty to the future needs of the business. Unlike a LOC which is short term and usually subject to annual renewal, a fully amortized loan, is only callable in the event of payment default.

A working capital loan also provides an advisor with knowledge of the loan process and proper use of debt, while familiarizing the lender with the practice, business, or firm (everything from cash flow to the valuation results), enabling all parties to be more responsive when the larger succession (or acquisition need) moves front and center. While it is certainly possible to "jump right in" during an acquisition or sale, a small, initial working capital loan makes an excellent, and practical, "trial run." This aspect underscores our previous point about working with buyers who are prepared and pre-qualified.

The size of working capital loans is situational. In most instances, these loans will be less than $350,000, an amount which can usually be expedited by our lending source's "small loan desk", with underwriting requirements further streamlined for loans of less than $150,000.

Apart from the reasons above, an initial working capital loan enables a practice, business or firm to address cash timing needs associated with its quarterly billing cycle. As well, in the context of internal succession, it sends a positive initial message to next generation advisors buying in that the business is committed to growth by adding a working capital facility to enable it to be more responsive to organic growth opportunities – and that the owner, or future owners, don't need to also be the sole financing source.

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