Financial Sustainability

Part 2: Setting-up your business finances

Produced through The Northern Rhode Island Conservation District 's ***Providence County Urban Growers Leadership Program***, in partnership with the Carrot Project and the RI Food Policy Council.

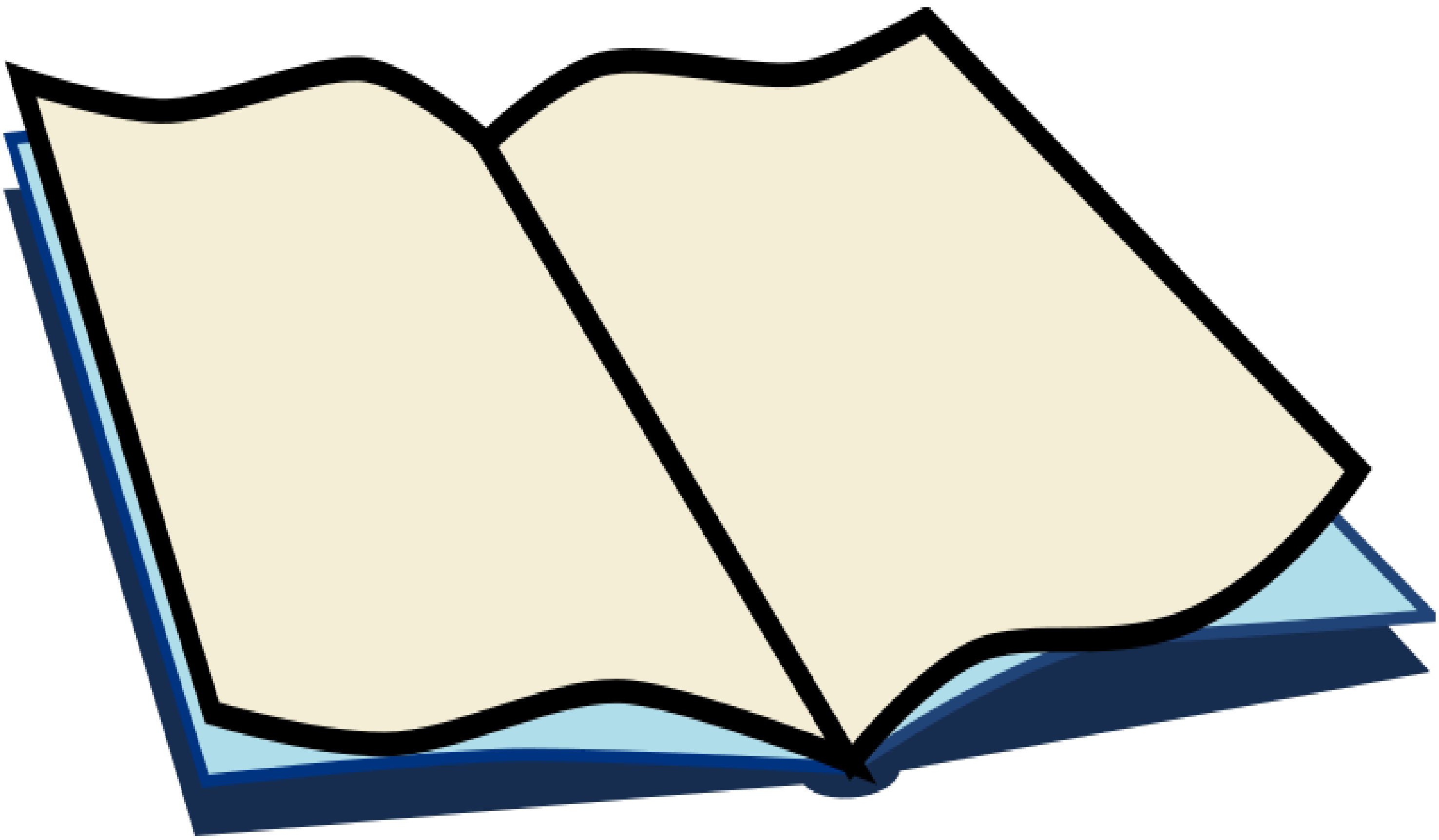
Table of Contents:

Produced through The Northern Rhode Island Conservation District 's ***Providence County Urban Growers Leadership Program***, in partnership with Carrot Project and the RI Food Policy Council.

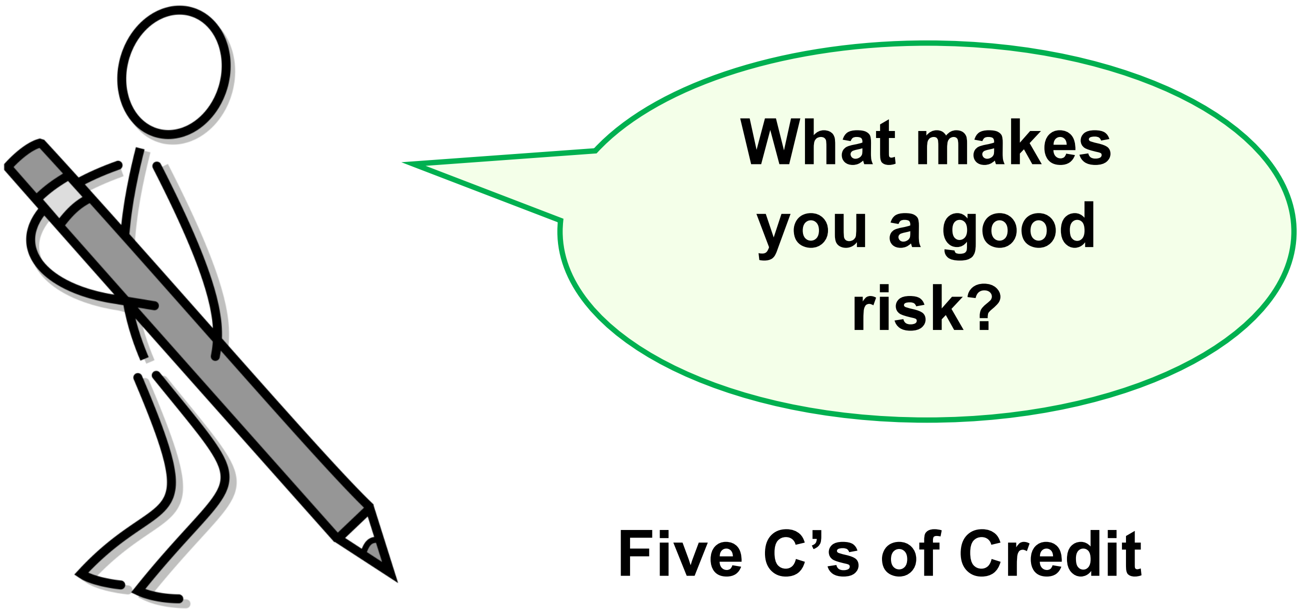
Preparing for Financing

Financing can come in many different forms such as loans, grants, investors, donors, etc. Preparing your financing can help set you up for success in searching, acquiring, and maintaining funding sources and keeping good records for your business.

You may have to conform to some pre-existing requirements to request and receive funding but you can develop your own systems to meet those requisitions.



Note: Even if you use your own capital to start or expand your business, you as an individual, are still loaning your business money. Preparing your finances for you to loan to your business is still very important to make sure you, yourself get paid back from the business.



Five C’s of Credit

1. **Character**

2. **Capacity to repay (cash flow)**

3. **Conditions / Covenants**

4. **Capital**

5. **Collateral** **(your current capital and infrastructure)**

For Agricultural business, the top three (3) are the most important

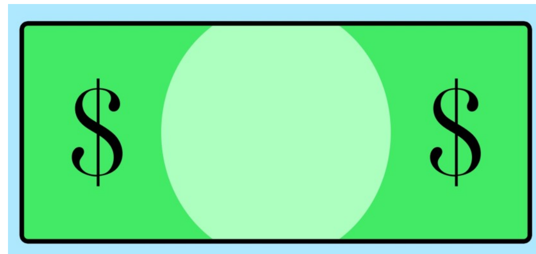
1. Character

Character is what you project yourself and the business as. Some questions to consider are:

- What is your role in society in relationship to the lender?
- How do they and the rest of the world perceive you?
- Have you defaulted on past loans or are you in good standing paying off your past loans?
- What about social media, how might that impact your loan and business?

2. Capacity to repay

Having enough money moving through your bank accounts to show you can repay the loan consistently.



<u>Determined by:</u>

- Current business cash flow.

- Future business cash flow projections (based on you business plan and your projected financials for your business plan) . They will look at your plans and determine if your future projections are realistic or not.

3. Conditions / Covenants:

A Condition of the loan is when there are stipulation that you and the funder agree upon. Collateral could be a condition of the loan. Some conditions could consider questions like:

- Do you own the land and/or the infrastructure of the business?
- Do you lease / rent? If so, is it a written lease? Is it a long-term lease?
- Is the equipment you have in good shape?

Convents of a loan are behaviors that the borrower must, or must not engage in.

Example of Condition and Convents:

A farmer leases land from the local Nature Conservancy with the convent being that they keep the farmland open, vegetated, and looking nice for the community. The farmer's farm plan might include a greenhouse to increase their growing season, address climate change, grow more valuable crops reliably, etc. The Nature Conservancy says that the farmer can not have the greenhouse because it violates their conditions of keeping the land open, vegetated, and nice for the community.

A condition / convent of the loan may be that if you default on it, there is something physically that you own that they can collect the debt on.

4. Capital:

Capital is the amount of productive capacity that your business has.

5. Collateral:

Collateral is any physical assets (s)of your business that a funder can collect upon as debt f you default on the funded agreement terms.

What makes you a good risk?

- Keep an updated business plan as time and your business progresses (so might your goals/objectives, and your financial plan).

- Having good financial records & projections (keep consistent / accurate recordkeeping!).
    - This is key to keeping track of your business for tracking success of your goals within your business plan and as the whole business. This is also key to showcase funders.

- A good relationship with a bank.

Fundamentals of good record keeping (books):

1. Pick a record keeping system:

Determine what record keeping system you want to use. Keep everything consistent. Once you pick one system and do not switch between systems.

<table>
<tr><th></th><th>Cash Record Keeping System (Cash Accounting)</th><th>Accrual Record Keeping System (Accrual Accounting)</th></tr>
<tr><td>Summery:</td><td>Makes manipulating your cash flow statement easier by recording revenues and expenses when the cash is received or spent.

Creates a financial statement of your business income and expenses that are based on actual dates of expenses and income of the business.

Takes only into account the current date of your financials</td><td>Allows you to create a business timeline that your income and expenses that go hand-in hand with one another. This will allow you to maintain a record of accounts payable (what you owe) and accounts receivable (what people owe you) by looking at expenses in the past/present, and your expected income in the future.

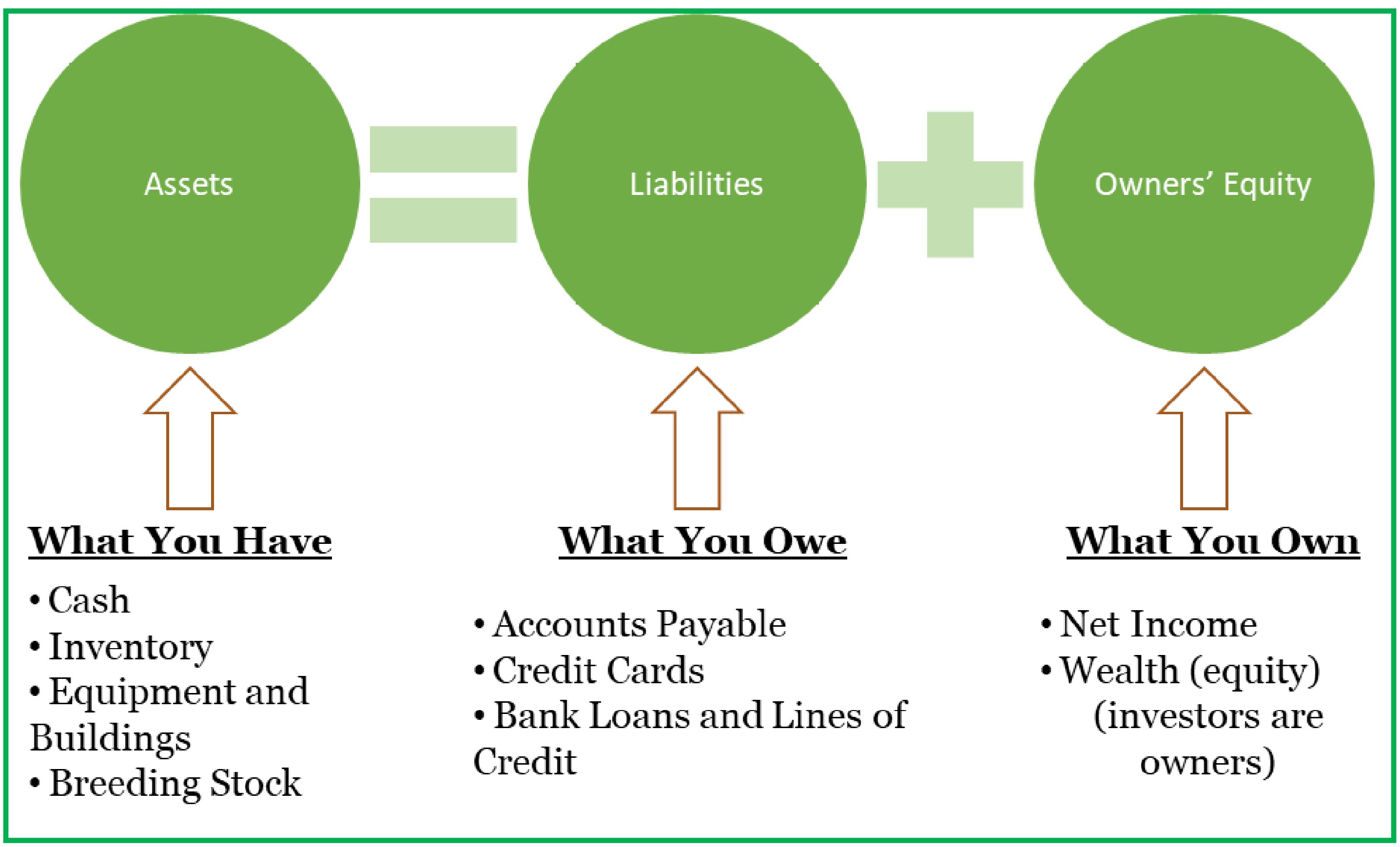
• Lines up your income and expenses so they are periodically within the same period</td></tr>
<tr><td>Example:</td><td>Your expenses and income are recorded at the time those exchanges happen. The expenses and income are not lined up in the same timeline, which can impact your cash flow statement because your income does not off-set your expenses right away.</td><td>Meaning, any initial expenses are not recorded the date of the expense, but rather the date that you receive income to off-sett the expense. This lines up your income and expense, cash flow financial statement in the same timeframe.</td></tr>
</table>

Fundamentals of good record keeping (books) (continued):

<u>2. Balance Sheet:</u>

Is a function of your books that showcase your assets, equity, and liability.

How you record your expenses for capital significantly impacts the view that you and your bank will see.



Fundamentals of good record keeping (books) (continued):

2. Balance Sheet (continued):

Example: You purchase a new greenhouse. How do you record your greenhouse? As an expense or an asset? (Think in terms of taxes)

As an Expense:

You show a lesser net profit and $0 in assets to you funder

Expense

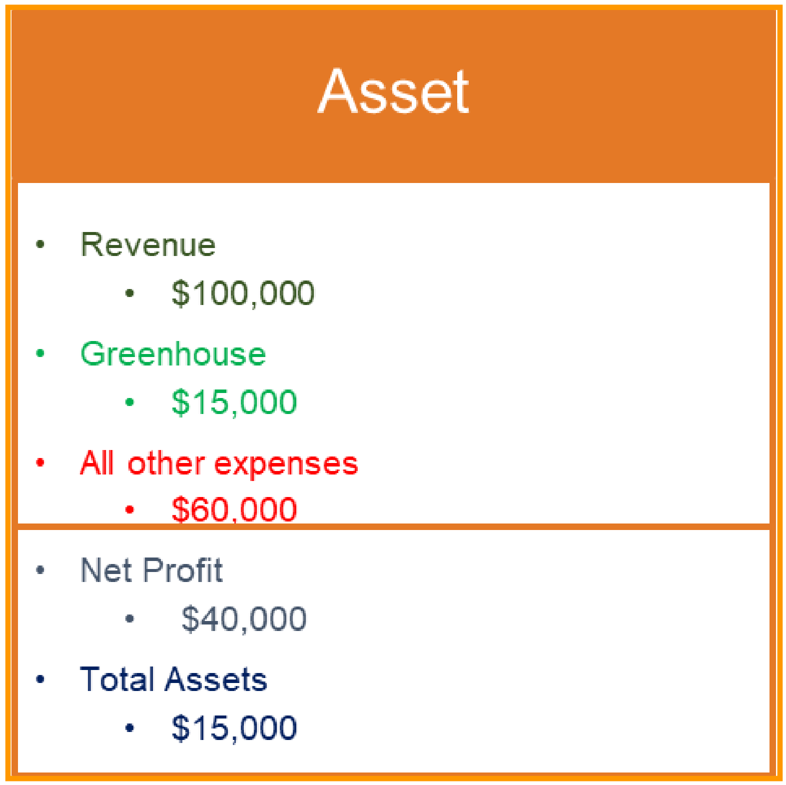
- Revenue
    - $100,000
- Greenhouse
    - $15,000
- All other expenses
    - $60,000

- Net Profit
    - $25,000
- Total Assets
    - $0

Fundamentals of good record keeping (books) (continued):

<u>2. Balance Sheet (continued):</u>

Example: You purchase a new greenhouse. How do you record your greenhouse? As an expense or an asset? (Think in terms of taxes)



As an Asset:

- In an accrual accounting system your accounts receivable get recorded under your assets and accounts payable get recorded under your liability. Therefore the business can use the terms of payment on your business terms (what are your terms, your timeframe you are expecting people to pay you) vs. cash accounting dictates your business terms for timeline and payment. Accrual accounting can manipulate your cash flow statement to have a more positive outlook on your business to outside funders.
- As taxes you record the Greenhouse as a capital expense. A capital expense is when you depreciate the value of a physical asset over time. Depreciation on capital expenses are calculated below net profits and total assets in your financial statement.
- Although you are still recording all your income and expenses. Your books don’t show the expense of the greenhouse. Keep in mind that your taxes will.

Fundamentals of good record keeping (books) (continued):

3. Cash Flow:

You will want to include your income and expenses of:

- Variable expense (something that changes with the volume of your production)
    - Example: labor based one how much production you are doing, cost of seed and fertilizer
- Fixed expenses (something that does not change with the value of your production)
    - Example: a greenhouse

Recommendation:

Creating a cash flow projection on a computer (excel or google sheets, etc.) where you can plug in the numbers and it auto calculates, reduces your time reducing/calculating projections, etc.

Patel Farm			
Income	**Jan**	**Feb**	**Mar**
Vegetable CSA	64,140	53,450	53,450
Egg Shares	5,200	4,800	2,402
Other Eggs	2,000	2,000	2,000
Chicken Shares	12,000	8,600	14,500
Other Chicken	4,635	4,635	4,635
	87,975	73,485	76,987
Expenses			
Variable	**Jan**	**Feb**	**Mar**
Direct Operating			
Fertilizer/Amendments	2,829	4,715	1,886
Seeds			
Fuel			
Pesticides/Chemicals			1,354
Field Supplies		327	
Wash Station Supplies			119
Animal Welfare (med supplies/vet)	158		158
Feed/Seed/Supplements	17,486	7,526	7,526
Housing			846
Fencing			
Delivery Costs	248	248	248
Slaughter costs			
Packaging			15,000
-			

4. Projections:

You take an existing set of records and change them based on your predictions on the future. With these projections you can set your financial goals of the business and see if your projections line up with your goals.

Fundamentals of good record keeping (books) (continued):

5. Consistent Practices:

Consistent booking gives you current profit and loss statements actuality. You know where your business financially stands today. It will give you accurate financials, and shows that you understand the impact your business is having on an outside funder and shows how a financial options (like a loan) would have on your business. This helps you keep good records and keeps you in good standing with the 5 C's of credit.

Ways of Financing:

Loan:

Is a sum of money generally from a bank, generally with a purpose, provided to you with an agreed upon timeline to repay the loan back with payments and interest for payments. You are required to follow the loan terms and conditions set out in the agreement. If the loan agreement repayment is not followed, a loan can have consequences specified in the agreement.

- Usually involves an application process that includes providing business financial details and projections to the lending institution
- May be temporary and partnered to anticipated cash inflow from revenue, a grant reimbursement, or both (called a “bridge loan”)
- The larger the loan, the more detail the bank will ask for

Ways of Financing (continued):

Line of Credit:

This is a different form of a loan that has a revolving credit. The credit is a pre-set amount that you can draw on at any time. When you draw on the money, they move the money from their account to your account and start charging you interest. Lines of credit do not expire and it can be accessed again and again.

Lines of credit can be used for a bridge loan. A bridge loan is when you use the line of credit as up-front funding to cover the costs of a project prior to receiving reimbursement for that project from another funding source.

Grants:

Grants are an awarded dollar amount given (generally a company, foundation, or government agency) to facilitate a particular goal. They are generally associated with a specific and discrete project and has particular requirements.

Grants are not free money. Grants provide you funding for projects. Keep in mind the reporting and time you must put into meeting the grant requirements.

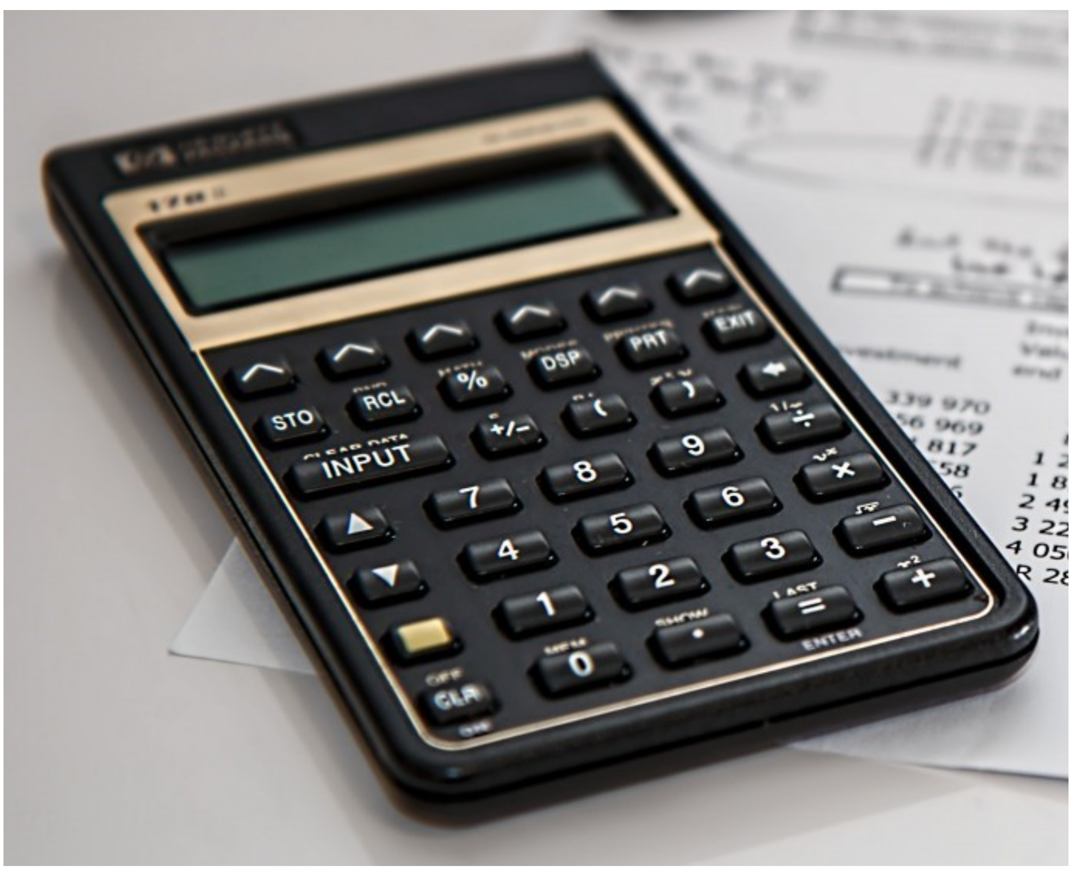
Investors:

An investor is person or company providing capital, often in exchange for ownership/equity. If you or and someone/group, puts money into your business, they are considered an investor. You may have to set-up a repayment plan. Formal/legal agreements are key.

Ways of Financing (continued):

<u>Alternative Investors:</u>

- All or nothing funding for a particular project
- Crowd-sourcing and other methods of utilizing private investments without losing ownership/equity. You have an obligation to provide a product to initial crowd sources later.
- Works the same way as other investors, but smaller $ amounts per person and no expectation of ownership.
- Third party generally hosts formal agreement and processing (i.e. kickstarter).
- A return of some kind is expected ('gift with donation of $ amount').



Making Yourself a 'Good Bet':

Loan:

Your ability to repay the loan amount on time.

Grant:

Your ability to fulfill the requirements set by the grantors. Consider the project from the grantors prospective—Will this investment support the goals of the grant program?

Individual Investor:

Will you be able to provide a return to them and will the investment support their goals?

Banking History:

- Good Credit
- Having money in the bank consistently
- Few overdraft fees or other low balance issues
- Getting a loan establishes a relationship with a bank. If you already have a re-existing relationship with the bank can help you secure your loan with the bank, weather it is your initial loan or another loan for your business.

Making Yourself a 'Good Bet' (continued):

Business Plan:

Anyone looking at you business to invest in will want to look at your business plan. If you as a business owner can't answer the questions (where it is?, where it will go?, and how to get there?), then it is not likely that you will reach your goals, and an investor will not be interested in investing with your business. An investor may also look at your plans for using funds. Such as:

- What will the financing purchase (assets, operating costs)?
- How will that affect your business (production and finances)?

Your business plan and financial records will showcase what is going on with your business, your goals, plans for the future, and demonstrates thorough consideration of everything.

Wish list Method:

The Wishlist Method is a spreadsheet of assets/expenses that you want to create for your business that you maintain. This is what you want to achieve in the future. This is a list of what you would need to purchase or do and those assets/expenses associated with each item on the list. This will help you easily and quickly prepare for future funding opportunities that may arise. This will save you time (and your monetary value of your time) preparing these financials when that funding opportunity comes about.

Finding Financing

<u>Loans:</u>

- Banks, Credit Unions, Community Development Corps
- Platforms like KIVA and
- Non-Profit Organizations: The Carrot Project
- Farm Credit East
- Government: SBA, USDA

Grants:

- RI DEM
- NRCS, SARE, USDA
- Local Organizations

Investors:

- KIVA – kiva.com
- Steward - gosteward.com
- Crowd Source
  - fundrise
  - Indiegogo
  - Startups: SeedInvest Technology.
  - Nonprofits: Mightycause.
  - Best for Investing: StartEngine.
  - GoFundMe.
  - Patreon.
- Local Organizations

Summary

- Focus on bookkeeping practice and projections
- Those practices will make you a 'good bet'
- Those practices will make it easier to apply for financing
- Stay connected through organizations like DEM, NRICD, RIFPC and the Carrot Project for financing opportunities

Get Support

- Sign up for 1:1 help
- Keep talking with NRICD
- Register your operation (farm) with FSA
- Rhode Island Small Business Development Center
- Connect with RI Food Policy Council

Produced through The Northern Rhode Island Conservation District ‘s ***Providence County Urban Growers Leadership Program***, in partnership with the Carrot Project and the RI Food Policy Council.