

Tap Family, Friends for Your Business Financing

Finding the funding to start a business often seems to be a daunting task. You can use your personal savings, but that may not be enough.

“Often business owners call looking for grant money,” says Glenn Muske, the North Dakota State University Extension Service’s rural and agribusiness enterprise development specialist. “The reality is that there are few grant programs out there to help someone start a business.”

“Probably one of the more common sources of capital, beyond your own, comes from family and friends,” says (Insert name) of (Insert title and county). “These individuals often express interest in seeing your business start and are the first ones willing to put funds up to make that happen.”

The financial support of family members has been, and will remain, an important source of business funding. It represents 87 percent of private financing for startup businesses, according to an estimate by researchers at Babson College in Babson Park, Mass.

This form of business financing often is labeled the “friends, family and fools” approach. It’s called that because the funding often is provided on a very casual basis, and the parties often are unclear if and when the money might be repaid. Such funding can be an easy way to ruin relationships.

Because financing provided by family and friends always will be an important funding source, treating such financing as a business transaction is crucial. The first step in doing this is determining the funder’s motives. Is the money a gift or a loan?

One common motive is the desire to have some management input, thus making the money an equity investment and not a loan. Business financing experts typically recommended that businesses avoid this type of arrangement because it can create future management issues.

Once you’ve explored the motives for providing the money, the next step would be to develop a formal business relationship. Here are some tips to help you do that:

- Develop a simple business plan and sit down with family members to discuss all aspects of the proposed business.
- Focus on a repayment plan that includes when payments will occur and the interest rate being paid.
- Draft an official agreement that includes the repayment plan and other important components such as early repayment, late or missed payments and how the loan will be paid if the business fails, and any special payment arrangements such as interest-only payments or no payments, perhaps during the first one or two years.

“Keeping the lines of communication open is important,” says (Insert last name). “Most of the problems in dealing with family financing often arise because of the lack of information. Remember that money changes everything in terms of family dynamics.”

Financing your business can be a difficult task. Help from family and friends is often the lifeline in the early startup stages. This financial assistance can be rewarding to the family and the business if done correctly.

For more information and tips about starting a business, contact your local Extension Service office at [insert phone number and email address]. Also visit NDSU's small-business support website at www.ag.ndsu.edu/smallbusiness and sign up for the monthly newsletter, or visit www.eXtension.org/entrepreneurship. The U.S. Small Business Administration and its related organizations, Small Business Development Centers and the Service Corps of Retired Executives, are also useful resources.

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For more information, contact glenn.muske@ndsu.edu or call (701) 328-9718. You also can visit our website, www.ag.ndsu.edu/smallbusiness.