

# **Borrowing from family and friends or peer to peer lending**

## **Part one**

Let's say you've got a great business venture and you're thinking about asking your friends and family for money. Other than the traditional and singularly ineffective approach, where do you start?

Today, we'll walk you through that process. We're going to show you how to paint the picture that sells the deal.

In past shows, we've talked in general terms about the mental processes of both borrowers and lenders. As you move forward to present your ideas to a lender, you have two important tasks. First, you need to have a very concise contained proposal.

I need \$12,000 to start a business. That's the traditional approach. The usual response is "Wow, how nice for you!"

However, if for example, you say

- "I have a new business that is being brought into the market. I've tried the concept a couple of times and it's been very exciting."
- "I've invested my own money to get this far and I'm running at about 30% of my estimated total capacity."
- "If I could get \$12,000 together. I could purchase a new widget maker (as we take a tip from business school story problems). That widget maker will allow me to capture the other 70% of the market that I can't serve now."
- "With that \$12,000 dollars, I'm going to buy the machine which costs \$8000. The installation, hiring the electrician and getting the concrete poured, is another \$4,000. I've got \$2,000 of my own money set aside for any overruns or anything like that."
- "I expect to be able to generate the necessary amount of money to allow me to repay this loan in 36 months."

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- “However, if I'm unable to reach that goal, my wife is working full time. With her earnings and mine, our family budget can support those loan payments if we need to bring it in at the 36 month deadline.”

This approach is vastly different from, “I need \$12,000.” The important part is that you've created a visible picture now. By telling a story instead of making a demand, you've really pulled the person into the opportunity.

Local lenders lend to make their communities better. Local lenders will be very interested in stories about you serving the 70% of the market that you're missing now. How will your growth make your community stronger?

For example, if you decided to start an oil change business, you can say, “How long did you have to wait for your last oil change? We can get you in quicker and everybody else in town.. I'm good friends with the people who run the other two shops. They're encouraging me to open because they hate scheduling customers out for weeks.”

Now you've tied the whole thing together for the lender. Your proposal is a concise and constrained proposal. You've got the market, you have the plan, and you've developed a relevant personal business network. You work closely within the market in which you will operate and you have commitment.

We remember I said effective pitching to family and friends needs to meet two criteria. The first is being concise and constrained, The second is to make sure your ask is of the appropriate size.

If your business currently has sales of \$1,000 dollars a month, asking for a \$60,000 dollar loan could be considered of inappropriate size. Lenders might say, “That's going to change everything about how your business is run. You haven't shown anything that tells us you can run a business 5 times bigger than the business you have now.”

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However, if you have a *supportable* need for a larger sum, it's still possible to put together a bigger deal. If you can support an ask of this size, consider working with a pool of lenders. This often happens with early stage investors. An attractive proposal has the potential to attract multiple lenders. Lenders sometimes like to spread out the risk of a business loan.

There's also some fun to be had here. There was a case in Skagit county where a person who owned a berry farm borrowed some peer-to-peer money. This borrower had a bigger ask and used three participating lenders. One of the lenders said, "You know I've been to your farm store and I love your blueberries. In our loan agreement. I would like two pounds of blueberries in July and two pounds in August as part of my interest payments!"

We've talked about the dangers of barter and how you can accidentally shoplift from yourself. However, if you think carefully and work out the numbers, these can be very creative and fun.

What do we do when we come to an agreement? Let's say you and the lender are on the same page. Oh, page means paper. Paper means getting the paperwork done. As is the case with all things having to do with money, you'd better get it in writing.

I hesitate to name the agreement because then everybody goes online and prints one out and thinks they've got it nailed and they don't.

When you go to your attorney to finalize the paperwork on this peer to peer loan, you might work on something called a promissory note or something similar, as recommended by your attorney.

The reason I don't like to talk about it too much is that first of all, I'm not qualified to give legal advice. Second of all, for a loan document to be effective and enforceable, it has to be written in a very specific way. You and your lender need to draft a document that is binding in court and enforceable by law. When money is talked

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about, people often get confused. With an enforceable written agreement, your lenders are protected and you are also protected, too,

Your loan agreement clarifies and makes very specific your responsibilities to your lenders. You also want to clarify your lenders' roles, so you can avoid what are called vest pocket lenders.

A vest pocket lender is a person who loans you a few thousand dollars then wants to sit in your 'vest pocket' and tell you how to run your business.

You can get a better understanding of prospective lender mindsets by talking to your lenders and learning about the lender perspective of your project.

Finally, your agreement should include a very clear lender exit plan. You'll want a clear understanding of when the loan is retired.

To sum up, you've put together a great proposal, you've drafted an enforceable agreement, you have a clear lender exit plan and you pay off the loan. Now your lender can put the money back in the community and help another business. If you find a need to borrow another round of funding in the future, you have the relationships, the tools and the track record to do it again!

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### **Part two**

This will be an especially fun show for me today. I often share my view that successful entrepreneurs have an attitude of gratitude and an abundance mindset. We also talk frequently about the importance of a personal business network.

Imagine my delight when a great example of these success factors landed in my email after our last show!

Last time, we talked about borrowing from family and friends and covered the seven secrets of peer financing success.

Let's review:

1. You are on the path to fundability with your personal credit in order and plenty of skin in the game
2. You can show the ability to pay a loan with your current revenue or second source of repayment
3. You are building a bridge, you're not filling a pothole, and you can bring a concise, contained proposal
4. Your ask is of the appropriate size for your business
5. You have a good Plan B, if the anticipated results don't materialize
6. You are willing to make a personal guarantee in the loan documentation
7. You have a clear lender exit plan

Of course, the unenumerated 8th success factor in borrowing from family and friends is finding someone from which to borrow. Normally, local peer to peer lenders are very hard to find.

Thanks to the power of our KONP signal, moving at the speed of light, with no subscription or data plan needed, a local lender who heard our show reached out to me via email. This is a real lender, right here in the KONP listening family, who wants to invest in our community by making loans to local businesses.

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### *What does that tell you about the power of networking?*

This local peer to peer lender had two questions for me, the first: Where are all the deals? That's right, this investor has money to lend, but can't find anyone who wants to borrow!

Of course, the answer to this question is a bit frustrating, for both borrowers and lenders. The deals, meaning businesses looking to borrow, are all around us. Not all of these asks are fundable, but many will be.

The problem is that most of these business owners are **working IN their business rather than ON their business**. When an owner is working IN their business, they don't have time for networking, attending meetings or even searching for information online. There is always one more call to make, one more issue to resolve, one more fire to put out.

The lenders are out there, but potential borrowers have made themselves too busy; working only *in* their business. Too busy to network and too busy to avail themselves of community resources. Resources who just might be a great source of business growth funding.

Working ON your business means making a plan to purposefully remove yourself from the day to day. These owners find ways to step outside of the operational and work on the inspirational. Even if it's only a few hours a week, that inspirational time, working ON your business, pays *huge* dividends.

Taking the time to seek growth funding is just one example, and a very good example, at that. You just might be the deal these local lenders are looking for.

Who is this person who reached out to me, you ask? If I told you, that would limit your options to a single potential peer to peer lender. How would you like to connect with a whole room full of potential lenders?

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This takes us to our listener / lender's second question, 'would I tell the listeners about a local lending group?'

Yes, yes I will.

This listener was referring to a loosely organized group of local people, with a common goal. That goal is to connect local lenders with local entrepreneurs.

This loosely organized group is called the Clallam Opportunity Investment Network, or COIN. COIN facilitates matching lenders who want to support their community with local entrepreneurs looking for resources to support growth.

COIN members believe in keeping funds local. COIN members believe lending locally delivers far greater community benefits than dollars working far away.

So, if you are an entrepreneur, or if you care about an entrepreneur, you might be interested in how you can connect with a COIN lender. The answer might surprise you.

COIN members meet entrepreneurs at events called business showcases. During a business showcase, a select group of entrepreneurs introduce their businesses to the audience.

This audience might include local stakeholders, economic development professionals, business advisors and, of course, COIN member lenders. If a lender is interested in meeting one of the presenting entrepreneurs, the lender will reach out to the entrepreneur to discuss options.

How do you find out about an upcoming business showcase? That's the fun part. You might remember that I said "...a select group of entrepreneurs introduce their businesses..." so, how do you get selected? You apply!

All of this information is already posted on my website, [kevinyourbusinesscoach.com](http://kevinyourbusinesscoach.com), but let's run through it quickly here. Visit the COIN website, [clallaminvest.com](http://clallaminvest.com), and

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follow the instructions for entrepreneurs. Next, complete your online submission. The online application is simple and user friendly, with just three questions:

Question one, 'Please share a brief personal background.' Your personal history, your business experience, your personal ties to this community, and the values that matter to you.'

Question two, 'Please give a brief description and history of your business. Include what your business does or hopes to do, who it serves, what needs or gaps it meets, and what benefits it provides to the community.'

Question three, 'What are you trying to accomplish with your business? What are the challenges and risks? What kind of support do you need to make this happen?'

COIN asks that you refrain from including financial information or requests for funding.

So back to the original question, when is the next business showcase? A business showcase is held when COIN receives enough qualifying submissions, so the date of the next showcase is up to you!

Thinking about that tourism business? Want to expand the business you already own? Would you like to buy an existing small business? This is a perfect time to build your abundance mindset. More applicants attract more lenders. Talk to your entrepreneur associates and encourage them to apply, too. We have the opportunity to enrich our entrepreneurial ecosystem right here at home.

COIN suggests connecting with the CIE or SBDC business counselors if you need free and confidential assistance with the application process.

- The CIE advisors, Rick Dickenson and Micah Jonet can be reached at [communityenterprise@cie-nw.org](mailto:communityenterprise@cie-nw.org) (360) 417-3421
- You can reach the SBDC business advisor, SharonAnn Hamilton at [SharonAnn.Hamilton@wsbdc.org](mailto:SharonAnn.Hamilton@wsbdc.org) and (619) 818-8575
- Visit [CLALLAM INVEST DOT COM](http://CLALLAMINVEST.DOT.COM) to learn more about COIN