



BUILDING YOUR BUSINESS CREDIT

By Stephanie Skaggs, Asset Financing Group, Inc.

Did you know that over 90% of all business loan applications are denied? In many cases, the denial, or “decline,” happened simply because the borrower didn’t know the underwriting guidelines used by the lender to approve loans.

Did you know that some lenders will deny your loan request if your business’s legal name does not appear in the 411 directory assistance? The loan request might also be declined if your business bank account balance is below a Low 5 (and what does “Low 5” mean?) Many lenders won’t even consider your loan request unless your business has five active trade accounts that report to the credit agencies (not likely if you are a new business). You might think you are an established business having been in business for over two years, whereas a lender considers your length of time in business as the length of time your business bank account has been open. A lender might require that your PayDex be 70 or above, whereas you have heard that your FICO score is above 680. The reasons for being declined can go on and on and you didn’t even know what criteria your business was being evaluated on.

Business owners need to build their BUSINESS credit rating and make it distinct from their PERSONAL credit rating. Unless the business credit is built separate from the personal credit, the business credit will be zero even if the owner’s personal credit is very good. Imagine if you were a 40-year-old woman and you had gone your whole life relying on your husband’s credit. You had never borrowed money and gotten credit in your own name. Then you find yourself in a situation where, you need to

finance a purchase. Would you be granted a loan? NO, because you have not established a credit profile. No credit equals bad credit in a lender’s eyes. The same is true for business credit.

Why does business credit matter, you still might ask? Because if you never build your business credit, then you will have a more difficult time in getting business financing; or you will pay higher interest rates and get worse terms, if your business doesn’t have a credit history. If you don’t establish it separate from your personal credit, your business credit will always be tied to you personally. For liability and growth reasons, someday you may want to have your business and you as separate entities. Financing can be a crucial part of growing a small business in the good times and keeping it afloat in rough times.

DON’T MAKE THESE MISTAKES

Some of the biggest mistakes business owners make in trying to establish business credit are often made without the owner even knowing it. Here are three frequent mistakes that business owners make.

Mistake # 1: Applying for Credit From the Wrong Sources

One of the biggest mistakes owners make in trying to establish business credit is applying for and getting credit from the wrong creditors. Did you know that there are over 500 business credit card providers in the US but only 60 will even consider approving your business credit card request without using your personal credit score and then requiring you to personally guarantee the

revolving debt? This is not a business credit card. This is a personal credit card with your business name on it. There is a big difference.

If the business credit card application is requesting the social security number of the business owner, then you know that the creditor is basing the request on that of the owner, not the business.

Mistake #2: Applying For Credit Where You Don't Have a Chance

Another big mistake business owners make is applying for loans in a scatter gun approach. **DO NOT APPLY FOR CREDIT FROM MULTIPLE LENDERS, VENDORS, OR CREDITORS WITHOUT FIRST KNOWING THEIR UNDERWRITING CRITERIA.** The quickest way to destroy your ability to receive business funding and to ruin your personal credit rating is by submitting loan applications to multiple creditors, who, in many cases, have no intention of offering you a financing package.

Do your homework. It takes work and time to learn who will give your business the best chance at receiving the right kind of financing. Call the company before submitting an application. Ask them their underwriting criteria.

Know your own credit scores, both business and personal. When applying for a business loan at a bank, tell the banker your scores and make sure he does not check your credit until after he has screened your loan request. Ask the banker, "Given that my credit scores are XXX (whatever your scores are), what is the probability of my request being approved, based on the other application criteria you see in my application?" If your banker can't give you an affirmative answer, look elsewhere before your credit rating is damaged from inquiries.

Mistake #3: Using Your Personal Money The Wrong Way

Most small businesses are initially financed by the personal savings or assets of the owners. However, in a growing business the personal assets or investments and personal credit often are not enough to sustain the business. It is necessary for the business to seek financing.

If done properly, the initial investment of personal assets can start the business off on a road to develop its own good credit rating. If you are working towards building a good business credit rating, consider this. Let's say you have \$20,000 to invest in a new business. You can deposit this money directly into the business or you could develop what's called "comparable credit" for the business. If you deposit the \$20,000 into your bank as a CD and borrow \$20,000 against it as a Line of Credit, you can start establishing business credit. Pick a bank that will report your payment history to the credit agencies. Your bank may even allow you to set it up so that the loan payments are made out of the CD. Later, when you need additional financing, other lenders will see that you have a great business credit history.

HOW TO BUILD YOUR BUSINESS CREDIT

Hopefully, by now, you will agree that establishing a business credit rating is important. Business owners must actively work to create a positive business credit rating. Now, let's learn how it's done.

Legal Business Entity

Of course, if you are applying for a business loan, you must have a legal business. This means that you and your business must be separate entities. There is no such thing as a business loan to a sole proprietor; this would be a personal loan. To obtain a business

loan, the borrower must be a business. Therefore, your business must be either incorporated (s-corporation or c-corporation) or be a limited liability company or partnership. None of these legal structures are difficult to set up. An accountant or lawyer can assist you in determining what structure is best suited for your business. You can also get help online at a number of websites such as www.mycorporation.com. If you are a do-it-yourselfer, you can get forms at your state's Public Regulation Commission Website. Creating a separate legal entity for your business is the first thing you as a business owner must do to build business credit and to separate business credit from personal credit.

Tax ID Number

Your business entity must have a Federal Employer Identification Number (EIN), which is like a social security number for a business. The EIN is also called the business tax ID number. You can obtain an EIN by submitting a request online at:

<https://sa2.www4.irs.gov/modiein/individual/index.jsp>.

Make sure that you obtain the EIN for your business using the EXACT LEGAL NAME of the business. In addition, obtain a state tax ID number, if your state requires this. Finally, make certain that you pay all the federal, state and local taxes that apply to your business including withholding taxes, gross receipt taxes and compensation taxes.

Physical Location

In order to establish your business as a real entity separate from yourself, it will need a separate, physical address, not your home or a PO Box. If you really operate out of a home office, rent a mailbox at a mailbox store that will give your business a physical address or rent space, even if it is just the

address, at an executive suite that will give your business a physical presence.

Business Phone Number and Listing

Professionalism aside, your business needs a separate phone and fax line. Conducting a business with the kids screaming in the background (unless, of course, you run a daycare) will not give your callers a professional impression. The business phone number must be listed with the 411 directory assistance under the exact business legal name. Lenders will often verify the legitimacy of a business by getting its phone number through directory assistance.

Business License(s)

Depending on the municipality, county, and state in which your business operates, you may need a business license. You may also need additional licenses to operate that are specific to your industry. Find out what agencies regulate your industry and follow their guidelines for operating a business. This is critical to building a favorable business credit rating.

Business Bank Account

To establish our business credit, your business must have its own bank account. Make sure that your business bank account is reported under the exact legal name at the same physical address as your business, not a PO Box or home address. Having a business bank account that is at least two years old would be great, but if you don't yet, work towards it. The best credit ratings come when your bank rating is a "low 5." Bank ratings are based on your average daily balance over the past three months. Here's how it works:

Score	Average balance over 3 months
Low 4	\$1,000 - \$3,999
Mid 4	\$4,000 - \$6,999
High 4	\$7,000 - \$9,999
Low 5	\$10,000 - \$39,999
Mid 5	\$40,000 - \$69,999
High 5	\$70,000 - \$99,999
Low 6	\$100,000 - \$399,999

Having an average balance in your business bank account of \$5,000 gives you a “Mid 4.” However, an average balance of \$10,000 gives you a bank rating of “Low 5” and many lenders will start looking at you. If you don’t have a Low 5, do what you can to save until you have at least \$10,000. You can even borrow from friends or family to place \$10K into your business bank account. You will never use this “borrowed” business money though. It will just sit in the bank to give your business a Low 5 Score.

DUNS number

The most common business credit reporting agency in the United States is Dun & Bradstreet (D&B), but Experian and Equifax also have business credit rating systems. Your company needs a “DUNS number” from D&B in order to build a credit rating with Dun & Bradstreet. Experian and Equifax do not require a special number. Having a DUNS number does not automatically mean your business has a credit rating. In fact, by just having a DUNS number but no other business credit information makes your business a medium

to high credit risk, even if you have paid all your business bills on time and as agreed.

For a D&B credit report, you can obtain a report at www.dnb.com for about \$50. They have a number of other reports that you can access, all for a fee.

WHAT’S YOUR RATING?

One common measure of a business’s credit rating is a “PayDex” score (a number between 1 and 100, the higher the number the better). PayDex is similar to a personal FICO score except the PayDex score is exclusively based on your business credit worthiness. A PayDex score of 75 is like a personal credit score of 640. The PayDex Score is calculated by using up to 875 payment “experiences” from vendors who report how your company pays it bills. The PayDex score card is provided below:

Score	Pay History
100	Early by 30 days
90	Early by 10 days
80	Paid as Agreed
75	Slow to 8 days late
70	Slow to 15 days late
60	Slow to 22 days late
50	Slow to 30 days late
40	Slow to 60 days late
30	Slow to 90 days late
20	Slow to 120 days late

In order to achieve a PayDex of 75 or better, you will need more than five trade references reporting to D&B with at least a total of \$15,000 in revolving credit that you

pay no more than a week late. For example, if your printing company gives you terms of “Net 30” (meaning they allow you to pay your bill within 30 days from the date of delivery) and they report to D&B (this is the key), this will start to build your business credit. This sounds simply but not all creditors report to D&B, in fact, not many do. Check with all your suppliers and ask them what terms they offer and if they report to the D&B. If your suppliers don’t report, ask them to do so, or you may need to find a different vendor. Retail creditors like Staples, Office Max, and Lowes issue business credit accounts and generally report to D&B. You might have to start with a very small credit limit while you are in the business credit building mode. This process takes time.

Know Your Business Credit Rating

Building good business credit is as important as establishing good personal credit. It takes time and effort, but it will mean you will be part of the less than 10% of business loan applicants who get the financing they want. Take the time to learn what lenders look for on loan applications. Make certain you have the criteria you need to get the positive response you desire. Pre-qualify yourself before you submit your information to a lender. If you can’t do this yourself, hire a consultant to look over your business qualifications before you hit the submit button. The results are worth it because you can obtain the credit you need and pay less for it, in most cases.

Stephanie Skaggs is a business financing specialist and consultant located in Albuquerque, NM. She has owned or managed several businesses and experienced many of the pitfalls associated with not having business credit. Over the past 10 years, she has been consulting with other business owners about developing business credit and preparing financing packages that get results. Stephanie can be contacted at Asset Financing Group, Inc., 4113 Eubank NE, Suite 200, Albuquerque, NM 87111, 505-856-1847 or Stephanie@asset-financing.com.

