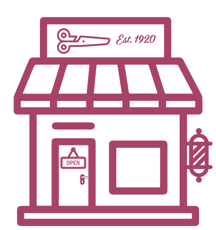
KAPITUS™

FINANCING YOUR BUSINESS

WITH A MERCHANT CASH ADVANCE

WHEN EVALUATING SHORT-TERM BUSINESS FINANCING OPTIONS...

a merchant cash advance may be one route to consider. This type of financing offers an alternative to traditional small business loans or lines of credit. In this guide, we explore the finer points of how an advance works and what to weigh in the balance when deciding if it's the right funding solution to pursue.



WHAT IS A MERCHANT CASH ADVANCE?

In simple terms, it's a way for a small business owner to borrow money in the short-term by leveraging future credit and debit card sales. Financing companies work with eligible business owners to offer them a lump sum of funding, based on the business's credit and debit card receipts. The advance is then repaid from those receipts on a daily basis, along with the financing company's fee.

The financing company chooses a specific percentage of credit and debit card sales to hold back as payment. The hold back amount may be anywhere from 10 to 40 percent. The actual dollar amount paid may fluctuate as daily credit and debit card sales increase or decrease. Payments are made automatically, typically through an Automated Clearing House (ACH) withdrawal from your business bank account.

HOW IS A MERCHANT CASH ADVANCE DIFFERENT FROM A LOAN?

Both an advance and a loan can provide businesses with a lump sum of funding. That's where the similarities tend to end, however. The key differences between merchant cash advances and loans lie in:

- Collateral Requirements
- Repayment Terms
- Fees and Interest
- Minimum Approval Requirements

First, let's look at how merchant advances treat collateral. A bank, credit union or online lender may expect you to offer collateral, such as business equipment or other assets, to secure a loan. With an advance, on the other hand, the financing company is more concerned that the business's future credit and debit card sales are sufficient to repay what's borrowed. Keep in mind, however, that the financing company may still ask for a personal guarantee as a condition of receiving an advance. This guarantee makes you personally responsible for the debt.

Next is how merchant advances are repaid. Rather than making one fixed payment weekly or monthly toward a loan, payments to an advance are usually made daily. The financing company takes the hold back right off the top of your credit and debit card sales.

While a loan may charge an annual percentage rate, a merchant cash advance carries a factor rate or factor fee instead. This fee, which we'll explain in more detail a little later, is used to determine the cost of the advance to your business.

Finally, merchant cash advance financing companies typically use different criteria to evaluate borrowers compared to the guidelines a bank or credit union may follow. While credit scores, time in business and revenue is considered, financing companies tend to focus more on the strength of the business's credit and debit card sales.

HOW MUCH CAN I BORROW WITH A MERCHANT CASH ADVANCE?

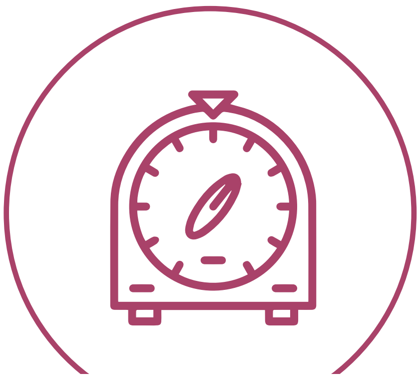
Every financing company caps borrowing limits differently. Broadly speaking, the minimum and maximum you can borrow may range from $2,500 to $500,000. The actual amount you'll be able to borrow depends on the lender you choose, your credit and debit card sales and your business's overall financial profile.

Compared to loans, the amount you can borrow with an advance is on the lower end of the scale. Some lenders, for instance, may offer up to $2 million in small business loan funding. The Small Business Administration's 7(a) loan program sets the bar even higher, capping the loan maximum at $5 million.

It's important to keep in mind, however, the merchant cash advances are designed to be a source of short-term funding. Hence, the lower borrowing maximum. That makes them better suited to meeting more immediate working capital needs for your business, versus investing in long-term growth projects or refinancing existing business debt.

PROS OF A MERCHANT CASH ADVANCE

There are several advantages associated with this financing option that businesses may appreciate. The chief benefits include:



Speed

Convenience

Accessibility

Compared to a loan, you're usually looking at a much shorter wait time between application and approval for a merchant cash advance. It's also a shorter leap from approval to funding.

You get convenience, in that there are no payment due dates to keep up with or payments to schedule. The financing company deducts payments for you automatically, so there's nothing you need to do other than process credit and debit card transactions as usual.

Most important, however, is how accessible merchant cash advances are to businesses that may have difficulty qualifying for other types of financing. Perfect or even fair credit isn't an absolute requirement; in fact, it's possible to get funding with bad or poor credit. We've already discussed that collateral isn't necessary, so there's no need to tie up any assets the business owns. Startups seeking capital may also find an advance is more in reach, compared to getting a term loan from a traditional lender.

CONS OF A MERCHANT CASH ADVANCE

On the con side, there are two things in particular that make merchant cash advances less attractive. The first is how they impact your business's cash flow.

Loss of Cash Flow Control

Expensive Borrowing Option

With a loan, you may have a set amount to repay once a week or once a month. Assuming you have a fixed interest rate, that payment is predictable. You also know what amount has to be paid, making it easier to forecast your cash flow and plan your business budget.

In a merchant cash advance situation, you lose some of that predictability and control over your business cash flow. While you may know that 10 percent of your credit and debit card sales are being held back, you have no way of knowing exactly how much your sales will be on any given day. This can make it difficult to estimate how much money you'll have left from your daily cash flow to apply to other business expenses.

The other side of that coin is that if you're borrowing money to meet working capital expenses, having to pay it back on a daily basis may add strain to an already tight cash flow.

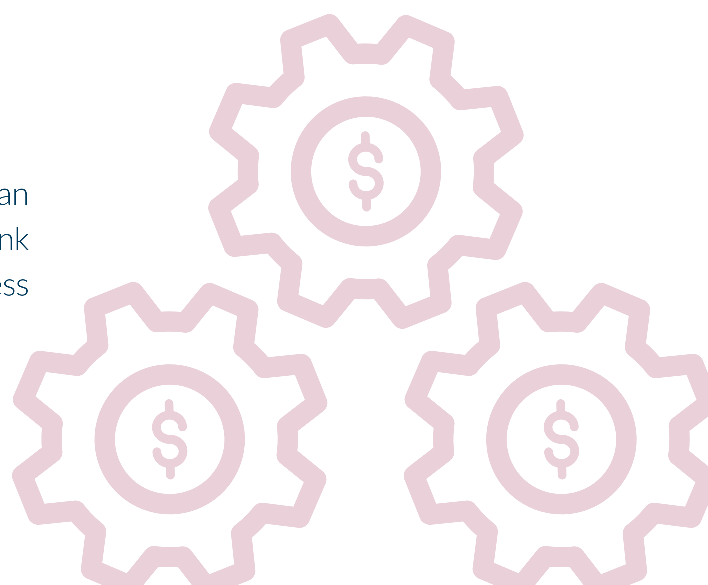
The second drawback is that merchant cash advances can end up being a much more expensive borrowing option than other kinds of financing. This has to do with the factor rate or fee and how the cost is calculated. While you're getting convenience, it's important to be aware that it may come at a steep price.

WHEN SHOULD I USE A MERCHANT CASH ADVANCE?

Technically, you could use an advance to meet virtually any funding need for your business. But you may find that it's more useful for handling these types of scenarios:

- Covering payroll or other basic overhead costs
- Purchasing inventory and/or supplies
- Meeting short-term expenses, such as your monthly lease or biannual insurance premiums
- Covering your outstanding accounts payable
- Paying for unexpected expenses

You might prefer to use an advance in lieu of a loan when you need financing quickly or you don't think you'll be able to qualify for a traditional business loan or line of credit.



WHAT IS REQUIRED TO GET A MERCHANT CASH ADVANCE?

Every financing company sets different guidelines for the minimum requirements for a loan. But generally, you can expect the financing company to take into account your:

Credit History

Business History

Finances

- Business and Personal Credit Histories
- Time in Business
- Average Annual Revenues
- Operating History
- Credit and Debit Card Sales

Of those five factors, your debit and credit card transactions are what the financing company is most likely to be interested in. Having strong daily sales may outweigh a low credit score or shorter time in business. In terms of where financing companies set the benchmark for credit, operating history and revenue, it can vary greatly.

For example, some financing companies might look for at least two years in business while others might only need you to be in business for three months. You may be able to get financing from one company with a 550 credit score, while another may require a score of 600 or better. That's why it's important to comparison shop when looking for an advance provider.

HOW QUICKLY CAN I GET A MERCHANT CASH ADVANCE?

Depending on the lender, you may be able to get the money deposited into your bank account in as little as 24 hours after being approved.

That's something that may be desirable if you need capital quickly and you don't have several days or weeks to wait for loan approval. For instance, you might be hoping to purchase some inventory while your supplier is offering it on sale. An advance would allow you to capitalize on that opportunity.

WHAT ARE THE TERMS OF A MERCHANT CASH ADVANCE?

The terms can vary based on several factors. Depending on how much you borrow and what's held back, you may be able to repay an advance in as a little as three to four months.

Some financing companies will let you extend that up to 18 or 24 months for a larger advance. As a general rule, the higher your hold back percentage, the faster you'll repay a merchant cash advance. Just keep in mind that repaying more from your daily credit and debit card sales means a tighter cash flow.

WHAT IS THE APR OF A MERCHANT CASH ADVANCE?

Merchant cash advances don't technically have an APR. Instead, the financing company charges a factor rate, which usually ranges from 1.1 to 1.5. This factor rate doesn't amortize the way an APR would with a traditional loan. Instead, you multiply this number against the amount borrowed to determine how much you'll have to repay.

Assume, for example, that you take an advance of $100,000, with a factor rate of 1.3. The amount you'd be responsible for repaying would be $130,000 ($100,000 x 1.3).

While there is no assigned APR, you can calculate an effective interest rate for a merchant advance. This calculation is based on:

The Advance Amount

The Total Payback Amount

Your Projected Monthly Credit Card Sales

The Hold Back Amount

So, using the previous example of a $100,000 advance with a $130,000 payback, assume that your hold back is 20 percent. Projected monthly credit card sales are $75,000. Using those numbers, the effective APR would be 76.92 percent, based on a daily payment of $500 and a repayment period of approximately 260 days.

The lower your monthly credit card sales, the lower the effective APR. But, the time it takes to repay the advance increases.

HOW MUCH DOES A MERCHANT CASH ADVANCE COST?

Aside from the factor rate, you may be wondering whether merchant cash advance financing companies charge additional fees. Unlike a loan, you typically won't pay any origination fees, late payment fees or prepayment penalties.

Again, the formula for determining the cost is straightforward. Simply multiply the advance amount by the factor fee to arrive at what you'll have to repay altogether. While you could also take the additional step of calculating the effective APR, remember that it's not necessarily a true measure of interest paid.

HOW DO I KNOW IF A MERCHANT CASH ADVANCE IS RIGHT FOR ME?

The answer depends largely on how much funding you need, what you need funding for, how quickly you need it and whether you're likely to qualify for other types of business financing.

Merchant Cash Advance

If you have a pressing need for capital, for instance, and your credit isn't great then a merchant cash advance could be your best financing option. The same may be true if you only need to borrow a smaller amount of money for the short-term and your business has strong credit and debit card sales.

Loan or Line of Credit

On the other hand, businesses that have good credit and require capital to fund larger-scale needs, such as opening a new location or purchasing expensive equipment, may be better served by a loan or line of credit. A loan could also be a better fit if you'd rather make payments weekly or monthly on a set schedule, versus making payments from daily cash flow.

HOW DO I CHOOSE A MERCHANT CASH ADVANCE PROVIDER?

When comparing merchant cash advance providers, first assess your financing needs. Then, use that as a guide to compare financing companies based on:

- Minimum and Maximum Financing Amounts
- Repayment Terms
- Factor Rates or Fees
- Funding Speed
- Minimum Approval Requirements

Also, consider the company's reputation and track record. Check the financing provider's rating with the Better Business Bureau and look for reviews or testimonials from previous borrowers online. Ideally, you should be working with a company that's reputable and offers merchant cash advance terms that align with what your business needs.

THE BOTTOM LINE

A merchant cash advance is just one way to fund your business. You can get financing quickly when you need it, even if your business is newer or you're working on improving credit. As with any type of business funding, just remember to keep the pros, cons and cost in perspective before taking an advance.

About Kapitus

Founded in 2006 and headquartered in NYC, Kapitus is one of the most reliable and respected names in small business financing. As both a direct lender and a marketplace built with a trusted network of lending partners, Kapitus is able to provide small businesses the financing they need, when and how it is needed. With one application business owners can save time and money, while eliminating the stress that comes with applying to different lenders. At Kapitus, we believe that business owners should be able to focus on running their business, while we take care of the financing. To learn more, visit www.kapitus.com.

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