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Seven Entrepreneurs in Search of a Deal

From new twists on time-honed tactics to the brave new world of Internet financing, here are strategies that can help land your business in the money.

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HOW TO FINANCE [almost] ANYTHING

From angels to local banks, from online investors to private-equity firms, persistent executives are finding the sources of money they need for their growing companies

1. For Growth

THE DEAL: $5.6 million raised through an online private-equity offering
THE ENTREPRENEUR: Sean Moshir, CEO
THE COMPANY: PatchLink.com, a provider of online software updates and patches in Scottsdale, Ariz.
REVENUES: $6.4 million
BACKGROUND: The company was founded under another name in 1991 as a provider of enterprisewide management software. It has grown to 25 people and has had positive cash flow for the past five years.

"Our original goal was to raise about $3 million," says PatchLink.com's chief financial officer, Robert A. Lettieri. "So I started contacting everyone that I could through my personal network from my prior experience with the capital markets.

"We started locally, trying to figure out who had an appetite for tech deals in Phoenix. But that base was quite thin. So then I reached out to people I knew in financing centers like New York and California. I must have contacted about 30 people I'd worked with in the past. But they were so busy that they weren't interested in deals of our size or in reaching beyond their local markets.

"We ended up getting term sheets for two possible investor groups out of Texas and Kansas. Those deals weren't very appealing, though. They were kind of egregious in what they wanted us to commit to, in terms of hurdles that we needed to achieve. Fortunately, someone that I knew introduced me to someone else who wound up suggesting that I talk to someone at OffRoad Capital [an online private-equity firm]. That was intriguing because they were really trying to do things differently."

CEO Sean Moshir picks up the story: "OffRoad liked us because we had a product-development track record that we could show to possible investors. And we liked OffRoad because they weren't just sticking to the same old venture-capital mode. Instead of a traditional road show, we did a live Web-cast one, which was great because potential investors could watch us and learn about our company in the convenience of their homes.

"The best thing of all about the process was that we ended up raising even more money than we expected to, without needing to give up any more of the company. If you have an initial public offering and you go public at $12 but the stock climbs to $40, your company doesn't get the extra cash from that run-up. But with OffRoad, because the sale was conducted like an auction, we ended up selling at $4.57, rather than $3.25 as we originally intended. And the difference went to us. Venture capitalists always try to sell you on their network of contacts. But the truth is, we didn't need it."

2. For Expansion

THE DEAL: $50,000 from an angel investor and a $150,000 seed-capital infusion from an early-stage venture-capital firm
THE ENTREPRENEUR: John Ferretti, CEO
THE COMPANY: Foxfire Printing and Packaging Inc., a printing company in Newark, Del.
REVENUES: $8.5 million
BACKGROUND: Ferretti founded Foxfire nine years ago as a traditional printer. It has been profitable and growing. He now aims to further increase his growth by diversifying into order fulfillment and printing services for Internet companies.

"I always believed that it made sense to build the foundation of my company, demonstrate that I could operate a successful business, and then look for ways that I could leverage that into more rapid future growth. So I didn't try to raise outside money for the first couple of years I was in business," Ferretti says.

"Still, I did concentrate on getting to know people and building a credible reputation for myself within my state's business and financing communities. One of the ways I did that was by helping to cofound Early Stage East, which is a two-day event that we host in Delaware to bring together entrepreneurs, venture capitalists, and investors. I know that if I had just approached these people cold as a guy who had a printing and fulfillment company, they might not have paid much attention to me. But my involvement in Early Stage East made it possible for me to start building some important relationships and to have a lot of conversations with different people about my company and my business plan and where I saw myself heading.

"I'm realistic. I knew that I didn't have the experience or the kind of company that would be able to bring in professional investors at the early stage of financing. So I concentrated on the angel community. The person who decided to invest in my company is an experienced businessperson who is interested in future liquidity, just as I am.

"We both hope that this company will be able to go public one day or merge with a larger company. Thanks to his funds and the additional investment that came in from the Delaware Innovation Fund [contacts with both that venture fund and the angel were made through Early Stage East], I've been able to pursue the Internet side of my business, which is what I believe will help us achieve the most profitable growth."

3. For Operations

THE DEAL: A $200,000 bank credit line
THE ENTREPRENEUR: Susan Ernst, copresident
THE COMPANY: Royal Electric Construction Corp., an electrical and telecommunications contractor in Columbus, Ohio
REVENUES: $5 million
BACKGROUND: Ernst and her husband purchased this 27-year-old company six months ago and have launched a growth strategy that depends, in part, on diversification through acquisitions.

"As part of our plan for growth, we acquired a small telephone and cable-installation and -maintenance contractor and needed a credit line to help us cover our operating expenses, which included new financing costs associated with that purchase. So I approached two banks: a large national bank and Commerce National Bank, a local bank that specializes in serving small businesses," says Ernst.

"It was remarkable how different those two experiences were. We gave both banks the same information and projections, but they handled it -- and us -- so differently! With the big bank, the employees we dealt with seemed to treat us like we were not important. There were very few phone calls from them. After we met with a loan officer, follow-up took a very long time. It was always, 'There's someone higher up who has to approve the deal.'

"With the local business bank, we got personal attention from the beginning. We felt as though they were entrepreneurs, so they understood us as entrepreneurs. Getting the loan approved was actually easy. After our meeting there was immediate feedback. By that I mean that within one week we heard that, yes, the funds would be available. And we also learned the specifics of the bank's terms.

"I'd urge small-business owners who have banks like this in their area to investigate them. It makes such a difference if you don't feel you're getting lost in the shuffle. I really feel that as long as we're fiscally responsible and hold up our end, this bank will be 100% behind our growth efforts."

4. For Inventory

THE DEAL: Up to $350,000 monthly in financing through a credit-card-company initiative to encourage small-business customers to charge inventory and raw-material purchases
THE ENTREPRENEUR: Herbert J. Mallet, CEO
THE COMPANY: Broudy Printing Inc., a printing company in Pittsburgh
REVENUES: $10 million
BACKGROUND: In the past Mallet used his personal credit cards to purchase company supplies, but he felt constrained by the $100,000 borrowing limits, and his accountant and lawyer strongly objected to his use of personal cards for business purposes.

"In my business, the biggest expenses are paper and other printing supplies. But I wouldn't want to use my bank credit line for those items -- why tie it up or make those purchases any more expensive than they already are by adding in financing costs? I believe in using my bank line only for major purchases, like a piece of equipment that I need to finance over 12 months," Mallet says.

"Using the American Express card for these purchases makes sense for me because it's a corporate card with effectively no limit, since my credit history is good. I always pay this bill off entirely at the end of the month. But using the credit card gives me up to 50 days of free financing. If you're talking about a $200,000 purchase of paper, that's a big float. And I save even more money because I discount my supplier bills by 2% to 3%, since I'm paying them within 30 days. It all adds up. You know why this also makes sense? When I get the credit-card bill, it might be three pages long, but we still need to write only one check. And the statements are a big help with our record keeping.

"The American Express part of all this was easy. The vendors were a little tough to convince, but the credit-card company helped us with them. I'd recommend this strategy to anyone, so long as his or her business isn't shaky. The truth is, if you don't have the cash flow to pay off your bills each month, and you get sucked into those penalties, you're going to wind up going down a dark, bleak road."

5. For a Web Launch

THE DEAL: $12 million from a group of venture-capital firms to finance a national product launch
THE ENTREPRENEUR: Stephen King, CEO
THE COMPANY: Virtual Growth Inc., in New York City, a provider of outsourced accounting and bookkeeping services
REVENUES: Undisclosed (75 employees)
BACKGROUND: King started this accounting firm in 1995 with $5,000 that his brother invested in the company, which King used to buy a computer and office supplies. During the next two years, he and his partners financed additional growth by maxing out their credit cards, refinancing a mortgage, and tapping into personal contacts.

"My goal was to raise $5 million from the venture-capital community, so I used my own network as well as those of our investors to develop a very selective list of prospects. I started approaching them in April last year," King says.

"What happened next was pretty amazing. One prominent firm, in conjunction with a major money-center bank, offered us $6 million but only on the condition that we agreed to raise another $4 million at the same time. Their logic was pretty simple: They didn't want me to be distracted by the need to raise more money later on, and they warned me that if I waited, I might not be able to get financing. They wanted us to be able to move aggressively ahead with our growth plan.

"I was completely overcome with joy and trepidation at the same time. After all, it was wonderful to think about not having to raise more money anytime soon. But as the company's largest shareholder, I knew that my personal holdings would face significantly more dilution if I agreed. I wasn't sure how to respond. So I went to our board. But they emphasized that this was my choice. I slept on it, and the next morning reached a basic conclusion: These guys are very smart -- in fact, they're smarter than I am when it comes to financing. They know what it takes to make this kind of growth happen. And if I agreed, I'd be done with fund-raising. I could get on with the things that really mattered to me and the company. So I agreed.

"The venture capitalists offered to find me the rest of the money, but I did turn that down. First, I wanted to try raising the money myself. And the truth is, once my other contacts knew that we had $6 million committed, there was a feeding frenzy. I had a dozen firms that wanted to get in on the deal. That's how we ended up with $12 million."

6. For R&D

THE DEAL: Private placements of $1.8 million in 1998 and $4 million in 1999
THE ENTREPRENEUR: Jim Reiss Jr., CEO
THE COMPANY: Coollogic Inc., in Dallas, which manufactures Linux-based Internet-access devices
REVENUES: Undisclosed (25 employees)
BACKGROUND: As experienced entrepreneurs who had previously built a technology company, Reiss and his cofounder, Rob Wood, were able to raise $500,000 for Coollogic from a private-equity firm *before* finalizing their incorporation. When the investment firm decided to divide its stake among its shareholders, Reiss and Wood ended up with about 1,000 accredited individual investors.

"We financed our earlier company through personal savings and then from some angel money and then brought in a venture-capital firm. But we were fairly disheartened by the time we left that company. We were in a minority position by then; we didn't like the way the venture capitalists were running things," Reiss says.

"With Coollogic, we took a situation that could have made things difficult for us -- suddenly winding up with such a big shareholder base -- and decided to turn it into something good. We made up our minds very early on that we were going to treat our shareholders the same way we would if our company were public. And we were going to make sure that our financial statements were accounted for according to the same high standards that we would need to meet if we were public. We thought decisions like those would help us to build enormous investor confidence.

"I made it a major personal priority that I would take every single call that came in from one of our investors. We frequently communicated new developments through shareholder letters. We wanted to make sure that people really understood what was going on with the company and where our growth prospects were. And because we were successful in building that kind of relationship with our investors, they really supported us when we went back to them for more capital.

"My partner and I have a completely different attitude with this company. We own less than 20% of Coollogic's equity, but that's OK because we're really building something of value here. Entrepreneurs make a big mistake when they think they have to hold on to 100% of everything. That's when they have nothing: they have zero value. They have a piece of paper, an idea that may never go anywhere. How do you wind up with something worth more? The only way is by partnering with people who have money and leadership and vision and can help you make it all happen. That's what's going on with us now."

7. For a Company Purchase

THE DEAL: A $592,000 Small Business Administrationbacked loan from a nonbank financial institution
THE ENTREPRENEUR: Masoud M. Anwarzai, president
THE COMPANY: Marathon Runner Courier Service Inc., a messenger service in Santa Rosa, Calif.
REVENUES: $750,000
BACKGROUND: Anwarzai bought this 30-year-old business last fall for $600,000 and needed to finance part of the purchase.

"When I bought my company, I knew that I would need financing, and my business broker recommended that I try Heller Financial because it's very active in the SBA-loan market. That was a good piece of advice. From the point at which I applied for the loan until we closed, it was less than 45 days," Anwarzai says.

"It really made a difference to be dealing with a loan officer who understood my needs as a small-business owner. Originally, I just applied for $450,000 -- which would have covered the financed portion of the purchase -- but she recognized that it would be helpful for me to have some working capital also. She helped the deal go through at a higher level, without any problems. Fortunately, the company's financials were strong, and my own credit history was good. It all went so smoothly.

"Was that surprising? Absolutely. But other good things happened as well. I really like the way the loan is structured. I've borrowed the money for 10 years, which seems like a reasonable time, but if I can manage to pay it off earlier, there aren't any prepayment penalties. That was important to me.

"Between the business broker who handled my acquisition and the loan officer, it actually felt as though my part was pretty simple."

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