LESSON

UNCONVENTIONAL BUSINESS NETWORK
ROUNDTABLES

LESSON 3: Business Performance

Business Structure And Funding Basics

Most people simply see the ownership structure of a business as a means to:

1. Avoid paying taxes,
2. Transfer any liability incurred during a businesses' ongoing operation,
3. Create personal wealth.

These are legitimate reasons for selecting the structure of the ownership of a business, but are they the most significant reasons?

Hand in hand with the business structure is how the business is to be funded in the beginning, and then on an ongoing basis. This lesson is designed to discuss some of the basics in business structure and business funding, but rather than looking at these important issues through the world's view, we desire to take an unconventional approach and consider God's view.

TYPES OF OWNERSHIP

To begin, it will be helpful to briefly review the various legal options for selecting a structure of business ownership.

Sole Proprietorship ■ This most basic form of ownership is where one sole owner has responsibility for the entire business. As such, the owner is not personally separated from the business enterprise, so while they are responsible for all liabilities and obligations, they gain all of the profits. Typically, most small retail and service-oriented shops are sole proprietorships.

Partnership ■ This is where two or more people go into business together acting as co-owners. This business structure is easy and inexpensive to create and is lightly regulated.

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Although there are several types of partnerships, the common distinction is that they decide how to share liabilities and profits among each of the partners. Often, this structure is the starting point for businesses that ultimately grow into a more advanced ownership structure such as a full corporation or franchise.

Corporations ■ This is a legal entity that is created to own and manage a business. The liability is limited among the owners but is taxed twice—once at the corporate level and once at the owner's profit-taking level. As of 2018, Walmart is the largest corporation by revenue in the world.

Limited Liability Corporations ■ This form of business ownership is taxed like a partnership, but the owners are shielded from liabilities as in a corporation. This type of structure is generally reserved for professional businesses, such as accountants and doctors, but can also be used for real estate ventures.

S Corporations ■ This is a special type of corporation that avoids the double taxation of a full corporation as all profits are passed on to the owners to pay personally depending on ownership levels. This form of ownership does offer limitation of liability as in a full corporation. S Corporations, however, have more restrictions such as the number and types of shareholders.

Franchise ■ This form of ownership allows a franchisee to borrow the franchisor's business model and brand for a limited period. The franchisee ownership in the business is regulated by the franchisor who maintains tight restrictions over ownership, training, quality and profits. Your local fast-food restaurant down the street is likely a franchise.

Co-operative ■ Co-operatives are organizations that are owned and controlled by an association of members. This is a rather democratic approach to business management where each member owns shares of equal value and everyone gets a chance to participate in the business decision-making process. Liabilities and profits are shared depending on the franchisor/franchisee agreement. Ace Hardware is one of the largest co-operatives in the world.

Private Equity/Venture Capital ■ This business ownership structure differs from the previous structures in that the participants in the business—the original creators, significant principals and vested employees—have little or no outright ownership in the business. The business is owned by a third party. Although there are a multitude of business models, in general, having a third party own your business means you will adhere to their demands, both good and bad.

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The choices of business ownership structures are extensive, with each having further variations depending on the business's locality and type. The common thread between each ownership structure, however, is how profits and losses are divided, who pays the taxes, how the owners are protected from liabilities and who gets to have a say in running the business.

DISCUSSION QUESTIONS

1. What is your business structure?

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   a. Why was this business structure chosen and has that rationale proven to be successful?

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   b. Do you foresee any reasons for changing your ownership structure?

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2. The previously listed business structures typically have more than one person involved except for sole proprietors.

   a. What benefits are there to additional owners?

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   b. What risks are there to consider when you add additional owners to a business? What are the additional risks in 50/50 partners?

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   c. How would you feel about those additional risks? How might you mitigate those?

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3. Read 2 Chronicles 20:35-37. Do you believe God cares about your ownership structure? If so, how should you respond?

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BUSINESS FUNDING

Once a business structure is decided, establishing a bank account for the new venture typically comes next. This requires a method or methods for funding the new business.

In 2015, The Kauffman Foundation surveyed companies identified by Inc. magazine as the 5000 fastest growing companies since 1996 to determine how they funded their business. The following chart shows the results for the different sources of funding and the percentage of companies using that source.

Source	Percentage
Personal savings	67.2%
Bank loans	51.8
Credit Cards	34.0
Family	20.9
Haven't used finance	13.6
Business acquaintances	11.9
Angel investors	7.7
Close friends	7.5
Venture capitalists	6.5
Government grants	3.8

While the results indicate multiple sources of funding, they can typically be classified into two categories: (1) equity or (2) debt. When you invest your own savings, it is typically going in to the business as equity, although it can be structured as a loan—from you to the company—to be repaid later.

When business owners don't have enough personal savings, typically a bank or credit card is their next option. When these possibilities are exhausted, they start leveraging their relationships with their family, their business acquaintances, their friends or others with whom they may have a connection.

Take a moment to examine the risks and rewards of these different types of funding.

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Debt

When business owners do not have enough personal capital to fund their entire business venture, they typically turn first to lenders. Although this can preserve their ownership position and their share of the profits, it does come at a cost in the form of interest or finance charges.

If interest rates rise, the loan payments increase, hurting cash flow and causing more risk for the borrower. We have been in such a low interest rate environment for so long, few have memories of the pain businesses suffered in 1981 when the prime rate at banks skyrocketed to 21% interest.

From God's perspective, debt is always a presumption on the future. When you sign the loan documents, you are presuming that your cash flow will remain adequate to repay the loan, but no one knows what the future might bring, except God.

Equity

Equity can come from you personally or it can come from others. When it comes from you personally, it may put your family's wellbeing at risk, but it comes with the lowest risk to the business. There are no additional shareholders or partners to contend with and no banks to whom you are beholden.

Once you have exhausted your own personal savings, you may find yourself seeking equity from family, friends or investors. They will typically either want their money set up as a loan, shifting into the debt category, or an equity in your business so that they can share in the profits. The rewards are that you may acquire the capital you need with a longer period of time before needing to repay it to your investors.

The risks, however, can be many. Depending upon how much equity is being provided, the investor will typically desire a percentage of ownership in the company. Many savvy investors do not like being a minority investor in a firm. Instead, they may leverage their investment to try to obtain controlling interest in your business. This scenario means you now work for them as opposed to being business partners.

The question and risk that few people seem to consider is, "What does God think about turning over a portion of His business to someone other than the person who was given the purpose or calling to start?"

A typical worldly approach by business owners is to determine how much money they need and then pursue all options possible to accomplish the goal. Very few ever consider that they are called to be a steward of the business rather than an owner, meaning they rarely consult with God on His preferred method of funding.

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LESSON

DISCUSSION QUESTIONS

1. How was your business originally funded? In hindsight, would you do it any differently?

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2. How do you feel about debt versus equity? How much risk are you comfortable taking?

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3. Discuss the spiritual pitfalls you may encounter in using too much debt or in having the wrong equity partner. Do you believe God can provide funding without requiring you to be in debt?

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4. Are there any steps you need to take to change your current business structure or business funding to be more in alignment with God's will?

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