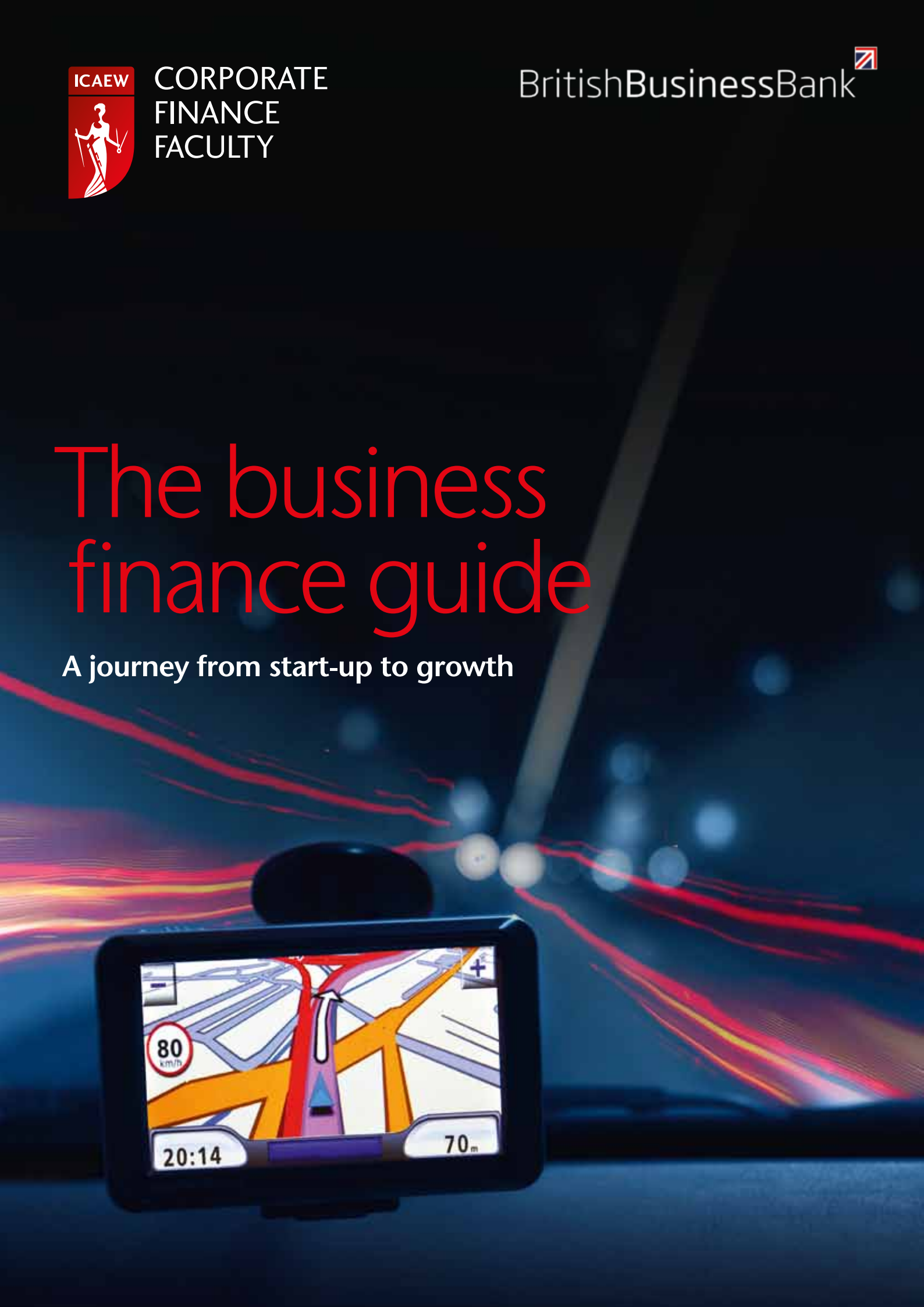
ICAEW CORPORATE FINANCE FACULTY

BritishBusinessBank

The business finance guide

A journey from start-up to growth



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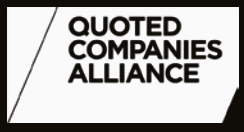

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ISBN 978-0-85760-920-5

Together on the journey

Small and medium-sized businesses play a key role in our economy, employing almost 60% of the private sector workforce and accounting for almost half of all private sector turnover. Their continuing success is vital to building the UK economy.

Being able to access the right type of finance at the right time allows these businesses to invest, grow and create jobs. A good understanding of the options available is an essential starting point and enables businesses to select the type of finance that is right for their circumstances and plans.

That's why the British Business Bank is jointly publishing *The business finance guide* with ICAEW's Corporate Finance Faculty, drawing on the considerable expertise of our partner bodies who represent both the finance industry and businesses themselves.

The guide sets out finance considerations and options for businesses at various stages, providing advice and sources of information to help them start, grow and prosper.

I hope that this guide gives businesses the information they need to capitalise on the increasing variety of available finance so that they can continue their journey to success.

Keith Morgan, Chief Executive, British Business Bank

'WE SHOULD NOT JUDGE PEOPLE BY THEIR PEAK OF EXCELLENCE; BUT BY THE DISTANCE THEY HAVE TRAVELLED FROM THE POINT WHERE THEY STARTED'

Henry Ward Beecher

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Introduction

Growing a business from the first seed of an idea is not a smooth linear journey and it's not as simple as a journey from A to B. The destination is seldom decided as the business idea takes form, becomes a reality and then grows into a successful enterprise. The finance journey is continuous; there may never be an arrival point.

For any business to travel on a journey it needs at all points of that journey to be appropriately financed. Businesses need to make sure there is the finance to back their growth plans. Businesses are often started on overdrafts or credit cards, or with help from friends or family or by using the family property as collateral. But soon after that the business will need to be financed so it can stand on its own two feet if it is to be a sustainably growing proposition.

This guide will be invaluable for entrepreneurs who are starting a business, directors who are running growing businesses and established companies – of all sizes – as well as for business advisers and investors.

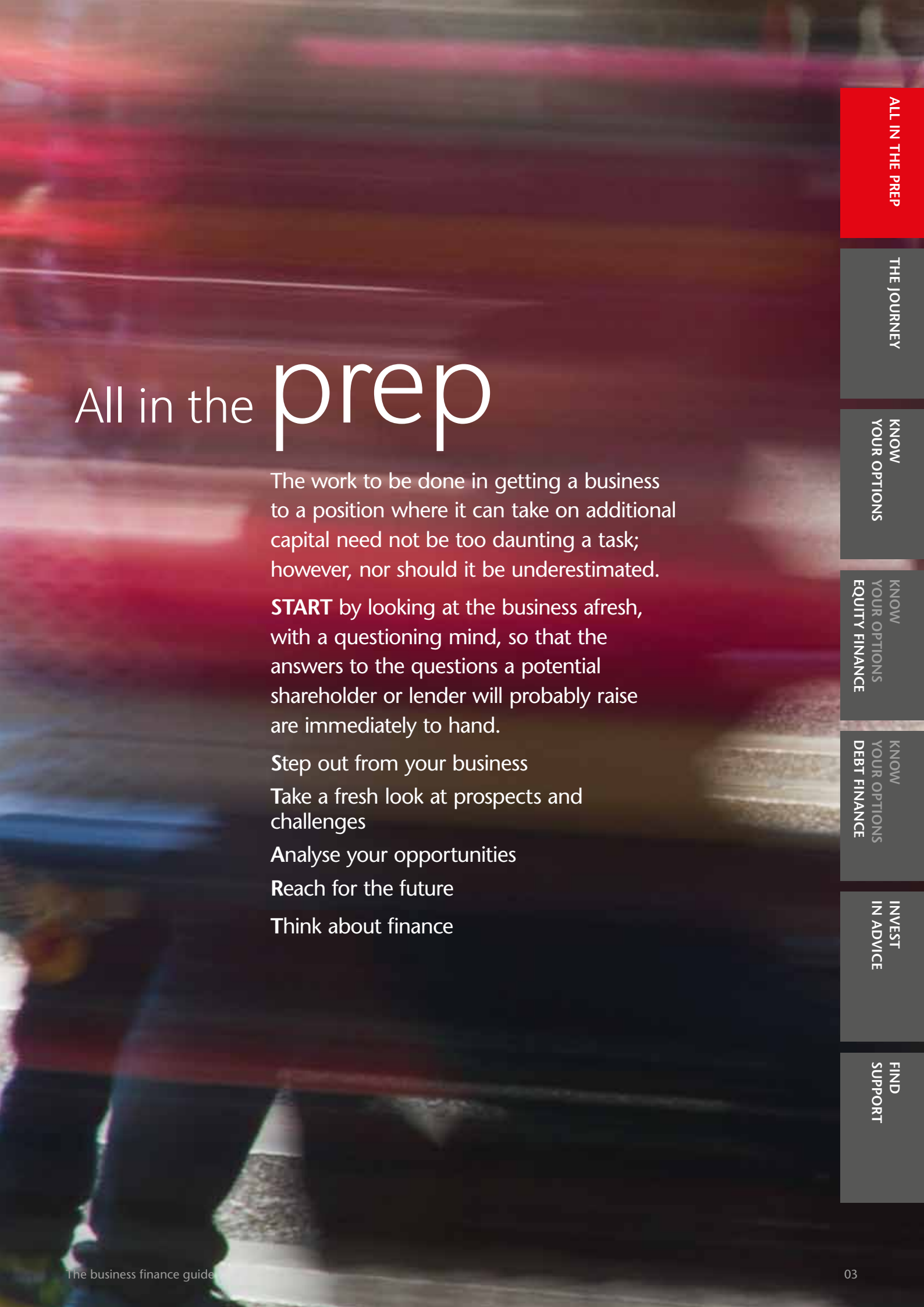
It explains how to approach the financing decision, the questions to ask and how to treat it as a business process, so that it is not as daunting as it can sometimes seem. And if it does get daunting, good advisers can provide further guidance. This guide also provides details of where to obtain free advice on raising finance.

Once a business is up and running on the growth journey, management will need to ensure that future plans for growth can be financed. If not, there is a chance the business will fail. The table on page 09 shows the options available to, and the decisions faced by, business-owners along that journey.

On the growth journey there will undoubtedly be ups and downs. Through the life of a business, as soon as plans are made, be they looking for growth or for survival or to batten down the hatches, the finance must be in place to support those plans.

'THREE COMPONENTS MAKE AN ENTREPRENEUR: THE PERSON, THE IDEA AND THE RESOURCES TO MAKE IT HAPPEN'

Dame Anita Roddick



All in the prep

The work to be done in getting a business to a position where it can take on additional capital need not be too daunting a task; however, nor should it be underestimated.

START by looking at the business afresh, with a questioning mind, so that the answers to the questions a potential shareholder or lender will probably raise are immediately to hand.

Step out from your business

Take a fresh look at prospects and challenges

Analyse your opportunities

Reach for the future

Think about finance

Step out from your business

Entrepreneurs want to focus on doing business. For many, finance falls under the category of administration, which may not be their forte. But to make sure the business can move forward they must step out from the business and ask the questions that need answering.

Take a fresh look at prospects and challenges

Plans may have been made when the business was little more than an idea. Things change and circumstances move on. You need to make a fresh assessment of where the business is, what the opportunities are, how achievable they are and what new challenges there are to the business.

Analyse your opportunities

You need to make a detailed analysis of the prospects for the business in light of any changed circumstances. A review of the new upsides and the new downsides needs to be carried out and the impact of them assessed, together with the probability of different scenarios.

Reach for the future

On the basis of the above analysis, prepare a detailed forecast, looking at the forecast profit and loss (P+L) account and balance sheet and then, crucially, at the cash flow, which will highlight how much capital needs to be put into the business to finance your latest plans.

Think about finance

You then need to think about the financing options for the business, how appropriate and how attainable they may be. To secure debt financing and/or investment, you need to make your business proposition clear and understandable to your target audience – with a business plan. At this stage a business is likely to require outside advice and experienced resource to ensure that it is 'investment ready' for potential investors, giving it the best possible chance to secure funding. Be open-minded. The funding landscape has evolved considerably over recent years and there are a lot of options available – some are new and some have been around for some time.

BUSINESS PLAN

Preparing a solid business plan is the key to securing funding. A robust business plan helps potential lenders or investors understand the vision and goals of the business. It also brings focus to management's understanding of the business strategy. It helps them understand the risks inherent in the strategy and the impact of any deviations from their plan – particularly when it comes to funding.

Information will depend on the target audience, but it should incorporate:

- an executive summary, highlighting the main points, designed to grab the attention of potential lenders or investors;
- details of key personnel, their responsibilities, skills and experience;
- market analysis of the company, its products or services and its competitors;
- details of current and intended client base;
- a marketing plan targeting new or existing customers;
- historic financial information covering the last three years of trading (if available) – accounts (audited if available), and key accounting ratios;
- cash-flow data, including information about standard payment terms and typical debt turn;
- financial forecasts for the next three to five years, presented as the historical information, and highlighting the key underlying assumptions;
- additional 'flexed' forecasts showing the impact of key downside scenarios, such as sales targets not being met or cost savings taking longer to come on stream;
- cash-flow forecasts covering the next two to three years (or in the case of a start-up or turnaround, until the business moves into profit), clearly highlighting the amount of funding required; and
- how creditors, capital expenditure, debtors and stock will be managed over the forecast period.

It must be clear how much of the existing owner's money is committed to the business. If a lender or investor thinks the existing owner does not have enough 'skin in the game', securing a loan or investment is likely to be more difficult, if not impossible. The business should consider whether investors would be eligible for tax reliefs (as described on page 12) and ensure that it communicates this in the business plan. The amount of any backing already received from other banks or investors must be clearly stated. This can demonstrate the attractiveness of the business as an investment.

If a business is looking for debt finance the plan needs to demonstrate how the business will be able to both meet interest payments and repay the capital element over the period of the loan. A repayment schedule linked to the forecasts will make this clear. And when looking for equity, the plan will need to show how the potential shareholder would receive dividends and how the value of the business and therefore their stake would grow.

The plan should always be 'fully funded' – with sufficient headroom so that the whole process will not have to be revisited too soon. Whether it is short-term debt finance or long-term growth capital, different equity investors and different debt providers will all have specific requirements when it comes to the content of business plans.

There is more detail on how to prepare a business plan on the websites of many of the contributors to this guide. Website details are on pages 22–24.

'THE BEST JOURNEYS IN LIFE ARE THOSE THAT ANSWER QUESTIONS YOU NEVER THOUGHT TO ASK'

Rick Ridgeway

CASH IS KING

Before looking for external capital, businesses should make sure they are managing cash effectively. Some fairly simple steps can help maximise available cash. Being able to demonstrate good cash management also sends out the right signals to potential investors or lenders.

The only way cash flow can be under control is by understanding the ins and outs. A weekly cash-flow forecast is often essential, particularly in a growing business.

Management must have an understanding of the amount of cash and working capital required to operate the business. Then working capital needs to be carefully managed. For example:

- stock and work-in-progress (WIP) levels must be reviewed, and excess stockholdings actively reduced;
- sales invoices must be issued in a timely manner and through best-practice credit management procedures, with payments collected within those terms;
- contractual agreements with suppliers should be reviewed to generate cash and suppliers paid to credit terms;
- capital expenditure should be carefully assessed and consideration given to the cash-flow implications of outright purchase; and
- automated payment methods should be used wherever possible – getting customers to pay by electronic transfer or through direct debit helps increase the speed and certainty of payment.

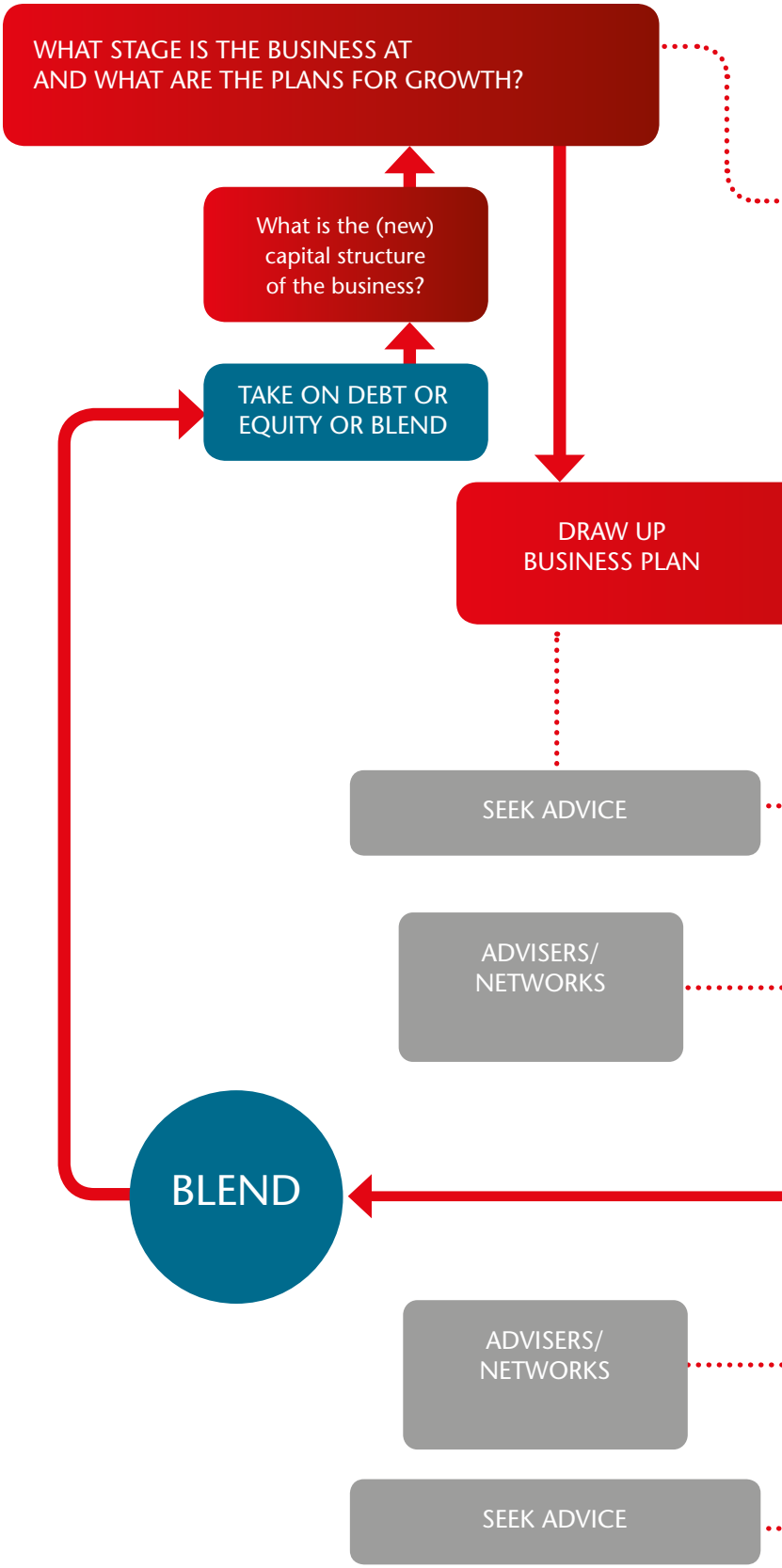
This approach to cash management is not just part of the preparation for taking on new investment or debt; it is a procedure that must be ongoing. With new stakeholders the scrutiny of cash flow will likely be even greater as the business's journey proceeds.

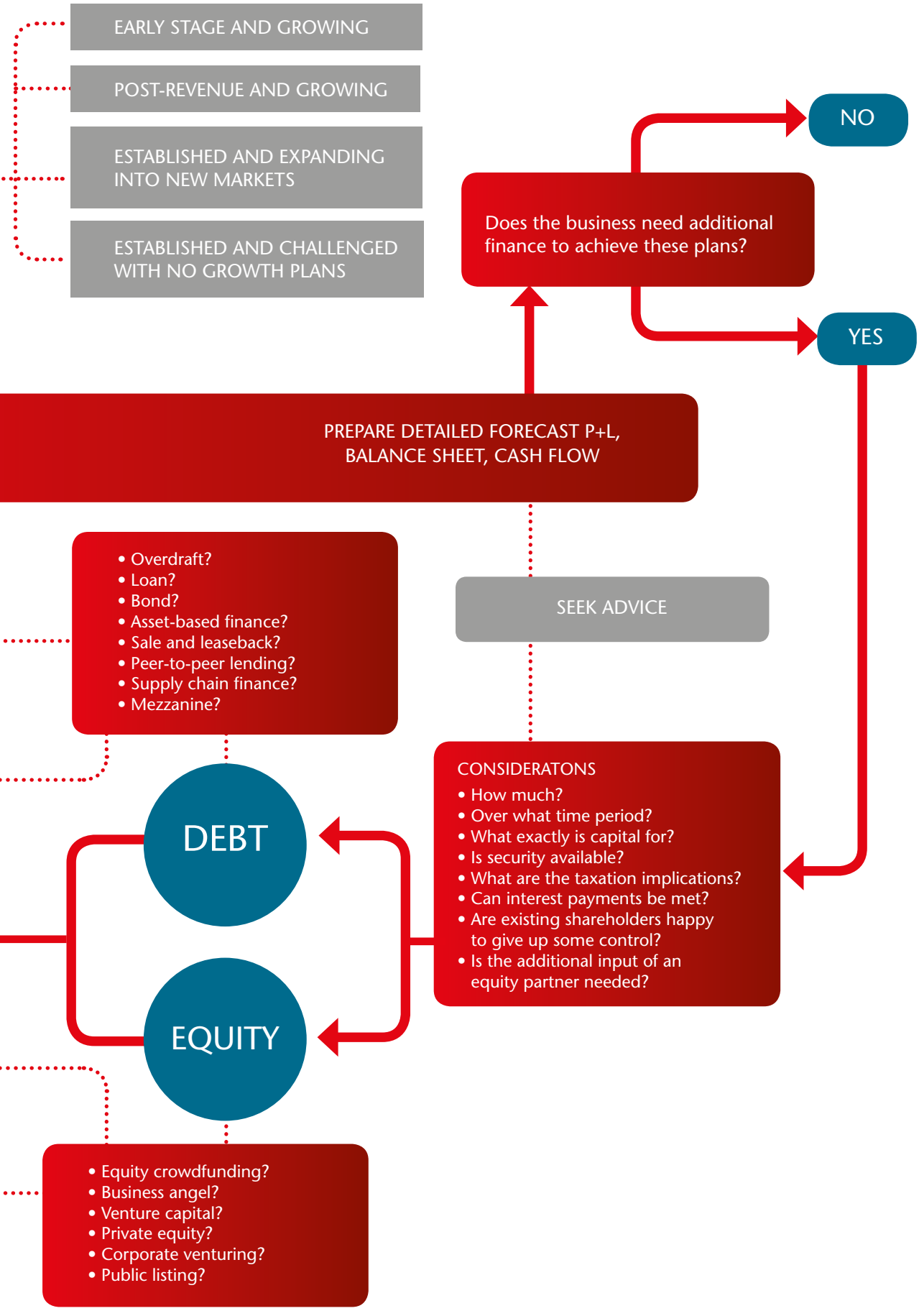
The journey >>

There are many instances where a business will be looking to take on debt and equity finance. Financing a business will often involve an injection of debt and equity. This table shows the financing cycle, which is not necessarily a journey that will end, and so involves continuous review and reappraisal.

'IT IS BETTER TO TRAVEL WELL THAN TO ARRIVE'

Buddha




EARLY STAGE AND GROWING
POST-REVENUE AND GROWING
ESTABLISHED AND EXPANDING INTO NEW MARKETS
ESTABLISHED AND CHALLENGED WITH NO GROWTH PLANS
NO
Does the business need additional finance to achieve these plans?
YES
PREPARE DETAILED FORECAST P+L, BALANCE SHEET, CASH FLOW
• Overdraft?
• Loan?
• Bond?
• Asset-based finance?
• Sale and leaseback?
• Peer-to-peer lending?
• Supply chain finance?
• Mezzanine?
SEEK ADVICE
CONSIDERATONS
• How much?
• Over what time period?
• What exactly is capital for?
• Is security available?
• What are the taxation implications?
• Can interest payments be met?
• Are existing shareholders happy to give up some control?
• Is the additional input of an equity partner needed?
DEBT
EQUITY
• Equity crowdfunding?
• Business angel?
• Venture capital?
• Private equity?
• Corporate venturing?
• Public listing?

Know your options

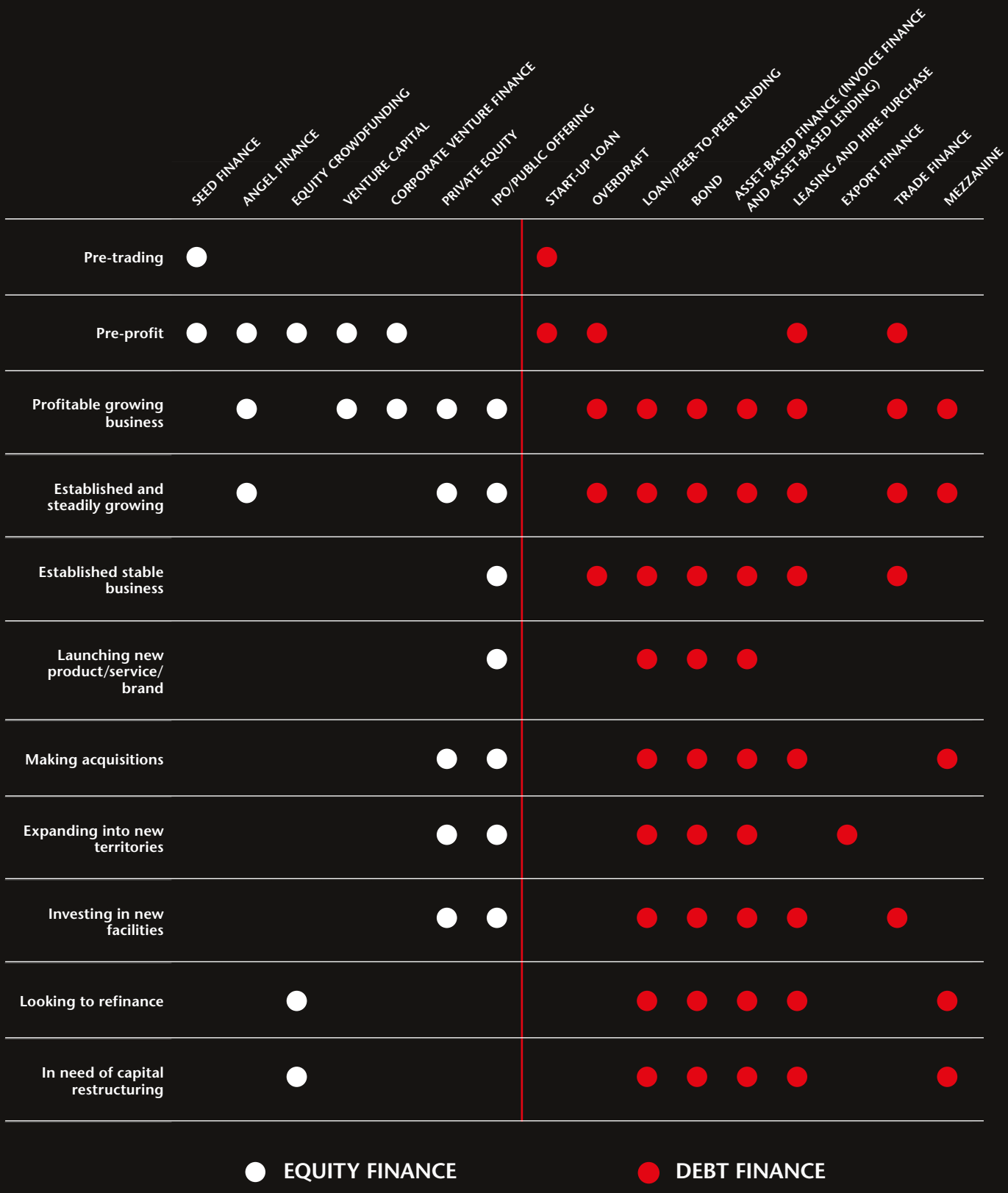
For any entrepreneur, wherever they are on their business journey, knowing what options there are along the way is key to making successful progress. And, crucially, this applies to the financing options.

The idea that an exact route can be mapped out for a business is one road analogy too far. Running a business will throw up many new challenges: closed roads or roads that lead to dead ends, so being aware of the alternative routes is critical. You may need to take advice on directions but if you are forearmed with the knowledge that there are alternatives, the journey is far less daunting.

This table shows the various options commonly available at different business stages. Availability will, of course, depend on the circumstances of a business.

'I HAVE NOTICED THAT EVEN PEOPLE WHO CLAIM EVERYTHING IS PREDESTINED, LOOK BEFORE THEY CROSS THE ROAD'

Stephen Hawking


SEED FINANCE
ANGEL FINANCE
EQUITY CROWDFUNDING
VENTURE CAPITAL
CORPORATE VENTURE FINANCE
PRIVATE EQUITY
IPO/PUBLIC OFFERING
START-UP LOAN
OVERDRAFT
LOAN/PEER-TO-PEER LENDING
BOND
ASSET-BASED FINANCE (INVOICE FINANCE AND ASSET-BASED LENDING)
LEASING AND HIRE PURCHASE
EXPORT FINANCE
TRADE FINANCE
MEZZANINE
Pre-trading
Pre-profit
Profitable growing business
Established and steadily growing
Established stable business
Launching new product/service/ brand
Making acquisitions
Expanding into new territories
Investing in new facilities
Looking to refinance
In need of capital restructuring
EQUITY FINANCE
DEBT FINANCE

Know your options:
Equity finance

You can look to equity investment as a way to finance many different stages of the business journey. Whether starting out or experiencing a high-growth phase, equity is an important part of finance arrangements for businesses and usually brings broader expertise with it. It is also important to recognise that many investors can take a minority stake – not purely a majority stake. Investors' interests are aligned with the business, meaning all are on board for the growth journey.

'THE ANGELS WHO BACKED MY BUSINESSES, BACKED ME FROM AN EARLY STAGE, THROUGH INTERNATIONAL EXPANSION, ALL THE WAY THROUGH TO FLOTATION. WE COULD NOT HAVE MADE THAT JOURNEY WITHOUT THEM.' Sherry Coutu

At an early stage, businesses will need a long-term backer who can fund the business through to revenue and profit – this could be through business angels and/or venture capital. In the shorter term, equity growth investment can support an aggressive growth strategy.

In simple terms, equity financing is the raising of capital through the sale of shares in a business. Equity can be sold to third-party investors with no existing stake in the business. Alternatively, equity financing can be raised solely from existing shareholders, through a rights issue.

Think about the future

You need to consider several issues before selling a stake in your business in exchange for capital. Here are the main advantages to a business of different forms of equity finance.

- Equity funding is committed to the business and its intended projects, even if plans change.
- Equity investors take a risk acquiring shares. In exchange they can see uplift in the value of their stake if the business performs well, as a result of the deployment of that additional capital.
- Investors have aligned interest with the business towards the pursuit of its growth and success. Its growth and profitability will increase the value of the business and therefore their shareholding.
- As well as taking a stake in the business, the right angels, VC investors or any other equity investor can bring valuable resource to the business. Their skills, experience and contacts can help with the development of the business strategy.
- If it is a private company, the business owner can sell their stake privately to a willing private buyer, or if the business is to be listed they can sell their shares through the flotation.
- Investors are often prepared to provide follow-up funding as the business grows.
- Public equity raising provides a liquid market, which can be accessed if further fundraising is required for future growth plans.
- Equity crowdfunding provides a company with wider access to capital providers among customers and the public.
- The crowdfunding process can be relatively quick.

Founding shareholders will have put the initial equity into the business. Friends or family may have 'invested' in the early stage of a business's journey, then business angels may take an equity stake. Venture capital (VC) investors (also known as venture capitalists), corporate venture capitalists or private equity (PE) investors tend to be the option for the growth phase. Financial institutions or the wider public may invest in equity through a listing of the company's shares. The public may also acquire equity stakes through equity crowdfunding platforms. It is not as simple as this in reality – business angels, for instance, invest at many stages of the business's growth. As it progresses, a company's shareholder register will be a mix of investors who have taken stakes at different stages of its journey.

Unlike debt providers or lenders (see the debt finance section), equity investors do not have rights to interest or to have their capital repaid by a certain date. Shareholders' return is usually paid in dividends or realised in capital growth. Both are dependent on the business's growth in profitability and its ability to generate cash. Because of the risk to their returns, equity investors will expect a higher return than debt providers. Where a project requires a longer-term investment than conventional debt will offer, equity will be the most suitable form of finance.

There is also a hybrid of debt and equity finance – mezzanine – that is covered in the debt finance section.

Other considerations for businesses looking for equity investment.

- Raising equity finance can be costly. It demands management time, which may be diverted from the day-to-day running of the business.
- Potential investors will scrutinise past results and forecasts of future performance, and will investigate background information, including that of the management team.
- The owner's share in the business will be diluted. And once the new shareholders invest, management will face varying degrees of influence when making major strategic decisions, of course depending on the nature of the shareholding and the stake acquired.
- Management time will need to be invested in producing regular information for the investor to monitor.
- There can be legal and regulatory requirements to comply with when raising equity finance.
- There are more disclosure and governance requirements if a company raises capital from public markets.
- Crowdfunds are normally 'fill or kill' – if a proposition does not hit its target it receives no investment at all.
- Dividend payments are not deductible for tax purposes.

BUSINESS ANGELS

Business angels are individuals who make equity investments in businesses with growth potential. They invest in businesses in the early stages of development, or post-revenue established businesses looking for expansion capital. Angels back high-risk opportunities, with the potential for high returns. Some invest on their own, others through an angel syndicate or club. However, the most significant trend is for angels to invest in syndicates or groups, generally with a lead angel. At seed stage, lower amounts of funding may be available. Businesses in the growth stage may be able to attract higher amounts from angel syndicates. Angels can offer multiple rounds of finance and frequently co-invest with other sources of equity and co-investment funds as further growth finance is required.

When taking on angel investment, a business should look beyond the capital they put in. Most can bring valuable first-hand experience of growing businesses, often early-stage businesses. Their skills and experience will be shared with the business, as well as their network of contacts. Most focus investments within a small geographic area, and so have local knowledge and local networks. Angels often make investment decisions quickly, without complex assessments. However, tracking down the right angel can take time.

Find out more through the UK Business Angels Association, **ukbusinessangelsassociation.org.uk**.

VENTURE CAPITALISTS

Venture capitalists invest in businesses with the potential for high returns – those with products or services with a unique selling point, or competitive advantage. They invest in a portfolio where a significant number of businesses may fail, so those that succeed have to compensate for those losses. They also want proven track records, and so rarely invest at the start-up stage. Like angel investors, venture capitalists bring a wealth of experience to the business. They are unlikely to get involved in the day-to-day running of the business but will often help focus the business strategy.

Securing VC investment can be a complex, costly and time-consuming process. A detailed business plan is a must. And legal fees will be incurred through the deal negotiation, regardless of whether investment is ultimately secured.

Corporate venture capital (CVC) is another growing source of funding for small businesses. It describes a wide variety of equity investment undertaken by a corporation, or its investment entity, into a high-growth and high-potential, privately-held business. CVC performs the same economic role that private venture capital plays – the identification and nurturing of the innovative businesses of the future. This formal and direct relationship is usually three-fold: by making a financial investment in return for an equity stake in the business; by offering debt finance to fund growth activities for an agreed return; by offering non-financial support for an agreed return, such as providing access to established marketing or distribution channels, or knowledge transfer. It is important that the corporation's aims are aligned with those of the business.

Find out more through the BVCA (British Venture Capital Association), **bvca.co.uk**, as well as its dedicated website on venture capital – **venturecentral.co.uk**.

HELPING HAND FOR INVESTORS FROM HMRC

When your business is planning for growth and you may be looking to take on equity, you may wish to make potential investors aware of three schemes from HM Revenue and Customs (HMRC). These are designed to encourage investment in unlisted growth companies through a range of tax reliefs against investment in new shares in those companies.

Enterprise Investment Scheme (EIS)
Businesses eligible to receive investment through the EIS must have:
- fewer than 250 full-time equivalent employees; and
- less than £15m of assets.

There are further requirements, which the company must meet for a continuous period from the issue of the share.

Seed Enterprise Investment Scheme (SEIS)
At the time of the new shares being issued, companies eligible to receive investment through the SEIS must:
- have fewer than 25 full-time equivalent employees;
- have less than £200,000 of assets; and
- not have had any EIS investment or investment from a venture capital trust.

Companies can receive a maximum of £150,000 under an SEIS.

Venture Capital Trust (VCT) Scheme
At the time the VCT invests in shares, an eligible company must have:
- less than 250 full-time equivalent employees; and
- less than £15m of assets.

There are further requirements, which the company must meet for a continuous period from the issue of the shares.

Companies can raise a maximum of £5m in any 12-month period from these three schemes. While they may be admitted to some growth markets such as AIM, they must not be listed on the Main Market of the London Stock Exchange or the ISDX Main Board and must be engaged in a 'qualifying trade' as defined by HMRC.

For further information visit **hmrc.gov.uk**.

PRIVATE EQUITY

PE makes medium- to long-term investments in, or offers growth capital to, companies with high-growth potential. PE investors would usually improve the profitability of the business through operational improvements and aim to grow revenue through investment in product lines or new services, or expansion into new territories. They will also typically introduce corporate disciplines and a management structure to the business, to give it a platform on which it can grow further. The PE model of governance consists of the combination of strategic, financial and operational expertise. The provision of non-financial support includes facilitating access to established marketing or distribution channels. PE investors would actively manage their investment through a period of five to seven years on average. After this they would exit their investment, selling their shares, having seen the value of the invested portfolio company grow. A PE firm may sell their stake to another PE firm or a corporate trade buyer. Alternatively, it may publicly list the company.

Equitable questions for an equitable outcome

Before seeking equity finance, consider these five questions.

1. How much is required?
2. What is it for?
3. How long will the funds be needed for?
4. What other skills does the business need?
5. What level of control do existing shareholders want to retain?

The answers can be incorporated in a comprehensive business plan, which should incorporate realistic financial projections, a detailed marketing plan and, crucially, what the investor can expect in return.

Networking and making use of any suitable contacts is critical to finding appropriate potential investors. Many corporate finance advisers will have networks of contacts in the business angel, VC and PE communities. Engaging an adviser can help the process.

Many private investors focus on specific industry sectors or geographical areas. The following associations may help you to track down investors, networks or networking opportunities:

- the UK Business Angels Association;
- the BVCA; and
- the European Private Equity and Venture Capital Association (EVCA).

EQUITY CROWDFUNDING

The use of equity crowdfunding by companies looking to raise equity finance is becoming increasingly common. In effect it is a means to connect companies with potentially hundreds of thousands of potential investors, some of whom may also be current or future customers. It does this by matching companies with would-be angels via an internet-based platform.

Raising equity finance through crowdfunding platforms can be an alternative to seeking angel or VC finance through more traditional routes – for start-up, early-stage and growth companies.

Before putting a pitch for equity investment on a crowdfunding platform, you would need to show that your business is investment-ready. As with attracting traditional angel or VC investment, you would need to produce a business plan and financial forecasts. A business might also include a video summarising the opportunity.

The fees payable for raising equity finance on the crowdfunding platform will typically be a success fee and legal fees related to the issue. You may incur additional legal and advisory fees in the preparation of the pitch. Limited due diligence is usually carried out by the platform and the investor may have the option to ask for more information. Although the investment will be listed on the platform, investors will not be advised to invest in a particular equity offering.

Find out more on the UK Crowdfunding Association website, **ukcfa.org.uk**.

The **British Business Bank** is encouraging diversity and competition in equity investment markets for smaller UK businesses by committing capital to investment funds. It does this through the following funds.

Enterprise Capital Funds are commercially-focused funds that bring together private and public money to make equity investments in high-growth businesses. The investment encourages venture capital funds to operate in a part of the market where smaller businesses are not able to access the growth capital they need.

The **Venture Capital Catalyst Fund** invests in commercially viable venture capital funds that might otherwise fail to reach a satisfactory 'first close'.

The **UK Innovation Investment Fund** (UKIIF) supports the creation of viable investment funds targeting UK high growth technology-based businesses.

The British Business Bank is also investing alongside business angels via the **Business Angel Co-Investment Fund (Angel CoFund)**, which supports businesses with strong growth potential, and the **Aspire Fund**, which supports equity finance investments in women-led businesses across the UK.

Further information on these and other British Business Bank solutions can be found at **british-business-bank.co.uk**.

PUBLIC LISTING

The next stage of growth for a business may involve applying for a public listing of its shares.

The UK markets are the London Stock Exchange Main Market, the Alternative Investment Market (AIM) and the ICAP Securities and Derivatives Exchange (ISDX).

The listing of shares would be a major milestone in a company's journey. The process is time-consuming, but it is an opportunity for a company to critically examine itself. The decision to launch an IPO (initial public offering) or flotation must be based on a realistic assessment of the business, its management, where it is in the stage of its development and its prospects. An application for listing requires the involvement of a range of advisers.

A listing may be used to raise money to:

- finance growth opportunities;
- finance acquisitions;
- rebalance the balance sheet;
- broaden the company's shareholder base; or
- provide liquidity at listing or when it comes to trading shares in the company.

The **London Stock Exchange's Main Market** provides companies with access to Europe's deepest pool of capital as well as the key benefits of higher profile and liquidity.

There are three types of listing on the Main Market. First there is Premium or Standard Listing. The former has stricter requirements, such as a 25% free float but both need a three-year trading record. Those ineligible for Premium or Standard Listing on the Main Market can access capital via the High Growth Segment, which requires a 10% free float and gives eligible companies the opportunity to fund their growth while preparing for an official listing in time.

A listing on the Main Market offers companies:

- access to a robust, real-time share price;
- access to deep pools of capital;
- benchmarking through the FTSE UK Index Series; and
- high profile through media coverage, investment research and announcements.

Find out more at **londonstockexchange.com**.

In addition, a public listing will often increase the profile of the company with a wide range of stakeholders as well as allow it to use its shares as an acquisition currency and to incentivise key employees through share option plans.

If your business has a trading track record and further growth plans, it would be in a position to raise equity capital through an IPO (flotation). A proportion of its shares would then be listed on a stock exchange and traded in the secondary market. An IPO is the sale of shares to institutional and larger investors and, sometimes, the general public.

The run-up to a company seeking a listing can be broadly divided into two phases – pre-IPO preparation and the IPO process itself. Pre-IPO preparation includes the critical review of a company's business plan and growth prospects, assessing the management team, appointing an appropriate board, tightening internal controls, improving operational efficiency and resolving issues that may adversely affect the listing early on.

When considering a public listing, a company should bear the following in mind.

- The **management team** will need to be able to explain the business, its strategy and prospects clearly to investors, and demonstrate knowledge of the market as well as its challenges.
- A comprehensive **business plan** will be needed, which will set out the products, markets, competitive environment, strategy, capabilities and growth objectives.
- The company's **financial performance** should preferably be one of consistent top- and bottom-line growth, with a sound balance sheet post-IPO.
- A financial model should demonstrate clearly the company's **growth prospects and associated risks** to give investors confidence.
- If the company is raising new capital, the **use of proceeds** should be clearly articulated and in line with strategy.
- Proper **financial controls** need to be in place.
- A publicly-listed company will need to clearly articulate its **corporate governance** arrangements to demonstrate it has a board capable of running a public company.

Listing shares will make certain ongoing demands on a company. Financial statements must be produced and corporate governance codes adopted. Quoted companies are subject to shareholder monitoring and there is always the possibility of a change of control. Generally, the actions of the company will come under far greater scrutiny, as one would expect when its shareholder base is spread wider and the public can potentially own shares in it.

Investor relations (IR) activity is the term used to describe the ongoing communication a company would have to undertake with the investment community. It is a mix of regulatory and voluntary activities and is essentially part of the public life that sees listed companies interact and raise their profile with existing and potential shareholders, analysts and journalists, customers and suppliers, and disclose information on new developments. IR activity requires a planned and strategic approach.

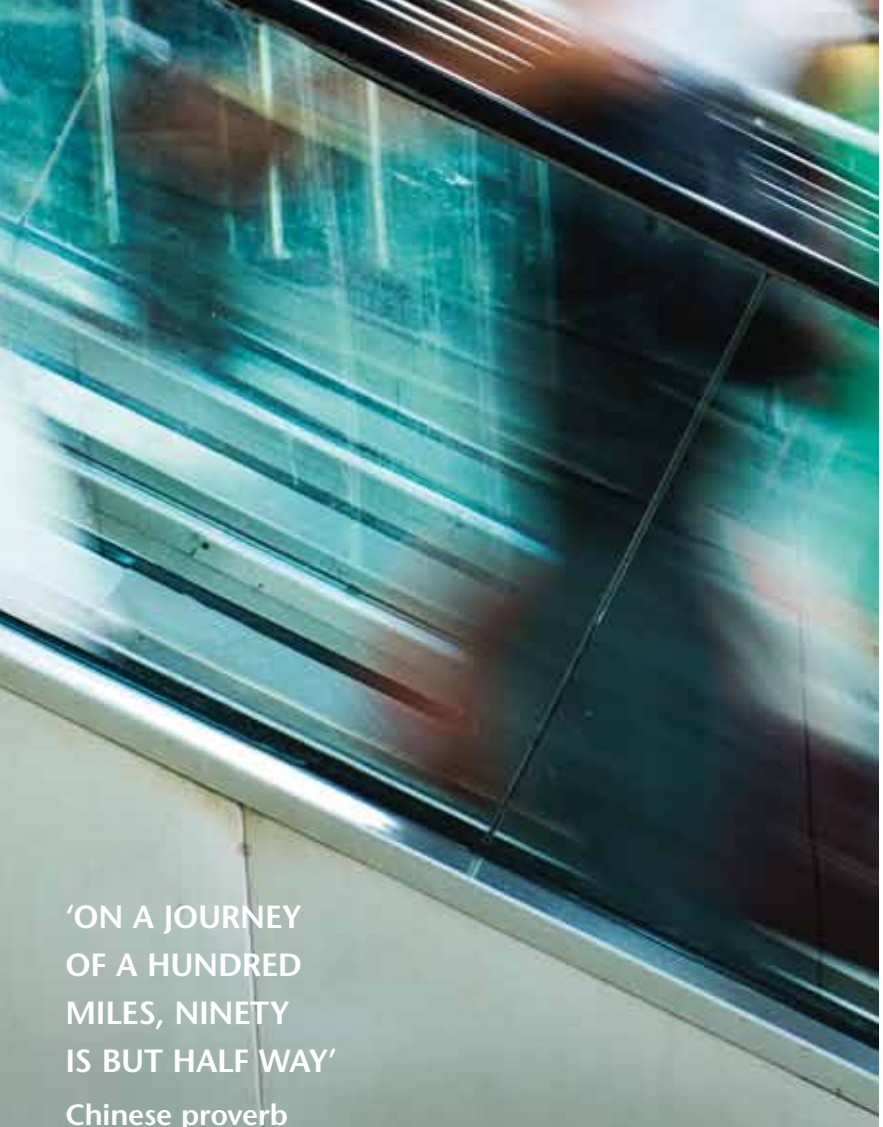
Once listed, there is then a ready market for the company to tap for further equity capital, through a further issue or placing, should it need further finance on its journey.

AIM is London Stock Exchange's market for smaller growing companies. AIM has less prescriptive eligibility and ongoing requirements than the Main Market and enables early stage businesses, including those with angel and venture capital backing, to benefit from a flotation on a public market.

ISDX is a London-based stock exchange providing UK and international companies with access to European capital through a range of fully-listed and growth markets.

The **ISDX Growth Market** is a source of equity finance for small- and mid-cap companies coming to a public market for the first time, as well as for existing issuers to raise further funds. Its admission process and ongoing regulation are designed to meet the needs of smaller companies.

The **ISDX Main Board** is an EU Regulated Market serving the needs of companies and other issuers seeking cost-effective admission to trading through the UKLA's Official List or other European Competent Authority.



'ON A JOURNEY OF A HUNDRED MILES, NINETY IS BUT HALF WAY'

Chinese proverb

Know your options:

Debt finance

Just as short-term capital should not be used to fund long-term plans, so the reverse is true. On the financing journey it is highly likely that you will need both, and the task is to get the mix right. Debt will undoubtedly be involved in growing a business. Debt comes in many different forms, each of which can be more or less appropriate to the type of business, the stage it is at in its development or the plans it has to grow. And often an established company will use a blend of different debt products from a range of providers.

Debt can be used for longer-term investment and/or to fund working capital. For the former, a loan, leasing arrangement or bond can be more appropriate and for the latter, some form of overdraft or asset-based finance (ABF) is likely to be more appropriate. At any stage of its development a business is likely to need a mix of the different available forms of debt. All have their advantages for different aspects of a business's growth plans.

Debt, in its simplest terms, is an arrangement between borrower and lender. A capital sum is borrowed from the lender on the condition that the amount borrowed is paid back in full either at a later date (a bullet repayment), multiple dates, or over a period of time. Interest is accrued on the debt and paid independently of the capital repayment schedule.

Unlike equity, debt does not involve relinquishing any share in ownership or control of a business. However, a lender is far less likely to help a business hone its strategy than a business angel or VC investor.

There are three broad categories of debt:

- loans and overdrafts;
- finance secured on assets; and
- fixed-income debt securities.

Loans from banks or other lending institutions primarily take the form of overdrafts or fixed-term loans. There are also peer-to-peer (P2P) business loans and start-up loans.

Finance secured on assets includes debt instruments such as asset finance (leasing or hire purchase) and ABF (invoice discounting (ID), factoring, asset-based lending (ABL) and supply chain finance). These are provided by most banks and specialist asset finance and ABF companies including some online platforms.

Fixed-income debt securities take the form of bonds or mini-bonds.

There are also community development finance institutions which provide micro-finance loans to start-ups and individuals as well as established enterprises. For further information visit **findingfinance.org.uk**.

What is most appropriate depends on the purpose of the capital being borrowed, the credit record of the borrower, the amount, the repayment term and the interest that is being repaid. You can see what is available from the different providers at **betterbusinessfinance.co.uk**.

OVERDRAFTS AND BANK LOANS

Overdrafts are often what a business uses to help day-to-day short-term requirements and as it grows incrementally. Loans, leasing or hire purchase agreements are in most cases better suited to larger longer-term purchases, such as investment in plant and machinery, computers or transport.

While it is almost always the case that an entrepreneur will benefit from the knowledge, insight and network of advisers who deal day-to-day with banks and other finance providers, businesses themselves should cultivate relationships with banks and other finance providers, who may help meet future financing requirements rather than just the immediate needs.

To obtain a loan or overdraft, management must prove to the lender that the business will generate the income and cash to both repay the facility according to the terms of the loan, and service the loan by meeting interest payments. Market conditions and regulatory requirements, such as those that mandate responsible lending to viable businesses, may also impact the ease with which a business can access a loan or overdraft.

It is likely that the business will need to provide security for any money borrowed against other personal or business assets.

PEER-TO-PEER LENDING

One major innovation going on in the supply of debt to businesses is P2P business lending. This is where internet-based platforms are used to match lenders with borrowers. The UK is at the forefront of innovation in this growing form of alternative online finance.

P2P business lending is a direct alternative to a bank loan. It can often be more quickly arranged and it will also allow partners, customers and friends and family who invest through the platform to share in the returns of the business. The minimum loan size is very small, which encourages a wide range of lenders to participate, and the maximum loan size of P2P business lending is growing.

Platforms have criteria on which businesses can borrow. They normally require financial accounts and a trading track record. Credit checks are carried out and lenders often bid for loans by offering an interest rate at which they would lend. Borrowers then accept loan offers at the lowest interest rate.

The Financial Conduct Authority (FCA) regulates P2P lending. P2P loans are to be eligible to be held in Individual Savings Accounts (ISAs) following consultation on the implementation details.

Further information can be found on the Peer-to-Peer Finance Association website, **p2pfa.info**.

ASSET FINANCE

This form of finance is used to obtain a wide range of items for your business – everything from telephones to vehicles – and could be the perfect solution if you need new equipment which would otherwise be unaffordable.

Because the loans are secured wholly or largely on the asset being financed, the need for additional collateral is much reduced and there is more security for the user because the loan cannot be recalled during the life of the agreement. Asset finance also offers ultimate flexibility because businesses have the option to replace or update equipment at the end of the lease period.

There are two main types of lease.

- A **finance lease** transfers all the rights and obligations of ownership to the lessee and can be for any length of time, but at the end of the lease the lessee will have paid at least 90% of the fair value, or market value, of the asset through an agreed schedule of repayments. The business will be responsible for maintaining and insuring the leased asset and it must be shown on the balance sheet as a capital item. Capital allowances can be claimed for leases over seven years long, and in some cases five.
- An **operating lease**, or **contract hire**, is appropriate if the business will not need the equipment for its entire working life. The leasing company will take it back at the end of the lease and is responsible for maintenance.

Asset finance is available directly from specialist providers or indirectly through equipment suppliers or finance brokers.

Most of the firms providing direct asset finance in the UK are members of the Finance & Leasing Association (FLA) and all their agreements would be subject to the stringent standards set out in the FLA's Business Code of Conduct. Find out more at **fla.org.uk/asset**.

ASSET-BASED FINANCE

ABF is a collective term used to describe invoice finance (IF) and ABL. IF includes factoring and ID, which will both involve funding provided against outstanding debts.

IF can be used to support cash flow and release funding for investment by generating money against unpaid invoices. IF is available to businesses that sell products or services on credit to other businesses. The funding provided tracks the growth in the business – increasing turnover unlocks more

- **Factoring** involves provision of finance via the purchase of invoices owed to a client by a financier, which can be either a bank or a specialist provider. The factor will advance the majority of the value of the invoices on notification with the balance remitted when the invoices are paid by the client. The factor works on behalf of the business – managing the sales ledger and collecting money owed by customers.
- In effect, factoring combines the provision of finance with a service element, helping the client with credit control, which can be particularly valuable for smaller businesses. **Export factoring** is also available which can support businesses selling internationally.
- Factoring can be provided on a **recourse** or **non-recourse** basis. The latter incorporates protection for the client business against bad debts.
- **ID** is similar to factoring, however, the client business retains control over the administration of the sales ledger. An invoice discounter would want to satisfy themselves as to the quality of a client business's sales ledger systems and procedures. ID can also be used to support exports.
- **Supply chain finance** (also, **reverse factoring**) is where smaller suppliers can take advantage of the credit strength of their larger customers. Supply chain finance requires the involvement of the supplier and their customer and up to 100% of the value of invoices can be funded once they have been approved by the customer, often at more competitive rates than would otherwise be available. Supply chain finance can be accessed directly through some larger organisations and also through a growing number of alternative providers.
- As with any type of finance, it is important to get advice on the legal, financial and tax implications before entering into any agreement.

ABL is a more sophisticated product and involves finance being provided against a pool of wider assets. These typically include debt, stock, property, plant, machinery and also potentially intangibles such as intellectual property or forward income streams.

Whereas IF would normally be provided on the basis of a purchase of the debts outstanding to a client, ABL would normally involve taking a charge over assets.

WEIGHING IT UP

Advantages of different forms of debt

- The terms can be tailored to suit the precise needs of the business.
- Repayments are straightforward, so can be simply planned for and the cash-flow impact budgeted.
- Generally, a loan costs less in interest than an overdraft over the same term.
- Overdrafts are often quicker to arrange than a loan.
- Interest is only paid on the amount of money used in an overdraft and the facility is only used if required – so they provide flexibility.
- There is tax relief on interest payments.
- Leasing gives a business access to the equipment they need without incurring the cash disadvantage of an outright purchase.
- Leasing is a flexible form of finance for all types of assets because the loans are secured wholly or largely on the asset being financed.
- P2P business lending can be more quickly arranged than a bank loan.
- The minimum P2P business loan size is very small, which encourages a wide range of lenders to participate.

Other considerations

- Lenders will always take into account a potential borrower's personal or business credit record when deciding whether or how much to lend.
- Loans are less flexible than overdrafts – charges could be payable on funds not used and there may be penalties for early repayment.
- Being locked into a rigid repayment schedule can prove problematic if cash flow is seasonal or erratic.
- Overdrafts are repayable on demand and so can be reduced or called in if the finance provider thinks that the business may be in difficulty.
- There are likely to be penalty charges for exceeding an overdraft limit.
- Security against the loan will almost always be required, as will personal guarantees from directors or owners.
- If a business is growing, the amount of asset-based finance will track the growth.
- Care should be taken when setting the repayment terms for a lease to ensure it is at least as long as the agreement.
- Interest rates in P2P business lending are often set by the market on the platform and reflect the level of supply of business loans.

BONDS AND MINI-BONDS

Bonds – retail bonds or corporate bonds – are a way for companies to borrow money from investors in return for regular interest payments. They have a predetermined 'maturity' date when the bond is redeemed and investors are repaid their original investment. Traditionally, corporate bonds and retail bonds would be traded on the stock market and really would only be available to larger companies.

Mini-bonds are similar but, crucially, they are not traded on a stock market and can only be promoted to certain types of investor. A lender is tied in until they mature.

The **British Business Bank** is enabling more effective and efficient debt finance markets for smaller UK businesses by providing guarantees on loans and loan portfolios, and by direct investment to support lending.

The **Enterprise Finance Guarantee** programme provides loan guarantees, encouraging lending institutions, including banks, to lend to viable smaller businesses that would otherwise be declined for lacking adequate security

Wholesale interventions (pilot) will provide guarantees on loan portfolios, helping lenders to unlock more lending to smaller businesses by enabling them to use their capital more efficiently, freeing up capacity.

Investment Programmes make commercial investments which stimulate at least the same amount of investment from the private sector, encouraging new lenders into the market and the growth of smaller alternative lenders, such as P2P lenders.

The British Business Bank also has oversight of the funding provided to the **Start-Up Loans Company** to administer the programme. Start-up loans help people start their own business, filling the gap where lenders are less willing to finance new start-ups. They combine a low-cost loan with free first class mentoring and support, both pre-start-up and once the business is up and running.

Further information can be found at **british-business-bank.co.uk**.

MEZZANINE FINANCE

This is a form of debt which shares the characteristics of equity but ranks below senior debt. Mezzanine is a flexible product that can be tailored to the risk and repayment profile of the business or transaction. It is typically used to finance the expansion of existing companies by VC investors. Basically debt capital, it gives the lender the rights to convert to an ownership or equity interest in the company if the loan is not paid back in time and in full.

Mezzanine finance is used in product developments, penetration of new markets, infrastructure investments or strategic merger and acquisition plans. As it can be structured with low cash coupons it can reduce the cash burden, so is particularly suited for high-growth companies where senior debt may be less appropriate.

EXPORT FINANCE

When businesses export, they need to be sure they can afford to produce the goods and that they will be paid. Export finance helps mitigate risks such as default or delayed payment.

Manufacturers who import raw materials face other challenges. Overseas suppliers want to be paid for materials before shipping, so the need arises for finance to fill the gap between importing the raw materials and the point at which the finished product is sold. That's where export finance comes in.

Export finance covers a wide range of tools, all used by banks to manage the capital required to allow international trade to take place as easily and securely as possible. Traditional tools are as follows.

- **Bonds and guarantees** – if the seller fails to deliver the goods or services as described in the contract, the buyer can 'call' the bond or guarantee and thereby receive financial compensation from the seller's bank. The types of bonds and guarantees include tender guarantee, advance payment guarantee, retention money guarantee, performance guarantee and customs bond.
- **Letters of credit** – these are issued by a bank, guaranteeing that the buyer's payment will be received on time and for the correct amount, assuming the goods (or services) have been supplied as agreed. If the buyer is unable to pay any or the entire agreed amount, the bank will cover the shortfall. The bank also acts on behalf of the buyer – the holder of the letter of credit – by ensuring that the supplier will not be paid until the goods have been shipped.

See also **gov.uk/government/organisations/uk-export-finance**.

TRADE FINANCE

Funding that assists businesses in purchasing goods, whether from international or domestic sellers, is termed trade finance. It is often transactional, with finance only being provided for specific shipments of goods and for specific periods of time. Here the asset being funded against is the goods themselves (as opposed to invoices in IF) and until repaid by the client, the goods belong to the finance provider. The process is supported by letters of credit, bills of exchange and bank guarantees.

Invest in advice

Corporate finance advice along the business journey is critical. Remember that it is advice and that good independent advice is invaluable. Advisers have experience of many businesses, whereas entrepreneurs may just have experience of the one they are in.

GOVERNMENT SOURCES OF INFORMATION

greatbusiness.gov.uk links to key sources of advice for businesses looking to grow, export and recruit.

gov.uk/business provides advice on starting, running, growing and financing a business, with an accompanying helpline available on:

telephone: 0300 456 3565
textphone: +44 (0)20 8742 8620.

gov.uk/business/business-finance-support-finder provides details on publicly supported finance, advice schemes, grants and loans.

ukti.gov.uk offers export advice to businesses looking to expand overseas.

BUSINESS MENTORING

Investment readiness may be the goal, but before a robust business plan can be prepared, the business may need access to knowledge and information so it can make the right finance choices.

Business mentors have both practical experience and a network of contacts to help businesses make the right choices. A mentor acts as an independent sounding board for ideas, provides guidance and support from a different perspective, and directs the business to the right areas for appropriate help.

mentorsme.co.uk is an internet-based mentoring gateway linking UK businesses who are looking for a mentor with over 27,000 mentors. The British Bankers Association manages the portal, working with its mentoring partners and more than 1,000 volunteer bank mentors offering expertise in financial support. All mentors can be accessed through the website.

BUSINESS COACHING

Coaching can help a business produce its business strategy and financial plan. Presentation training is extremely useful in helping management present the company and their plans in the best possible light. It prepares them for the rigorous scrutiny of those plans by potential lenders or investors. At this stage an adviser would be comfortable introducing the company to a network of investors or lenders. Many independent advisory firms offer mentoring services.

ICAEW's Business Advice Service offers help to businesses in England, Scotland and Wales to overcome the challenges they face, including:

- how to grow a business;
- **securing loans, capital and finance;**
- keeping staff and creating new jobs;
- meeting tax and regulatory requirements;
- export planning;
- **planning for long-term sustainable growth;**
- **debt management;** and
- legal issues.

Businesses are offered a free advice session with an ICAEW Chartered Accountant. Visit **businessadviceservice.com** to find the nearest office participating in the scheme.

GrowthAccelerator is a unique service led by some of the country's most successful growth specialists to provide business coaching. Coaching is provided by a private-sector consortium led by Grant Thornton and comprising Winning Pitch, Oxford Innovation and Pera and is backed by government.

Coaching is not prescriptive – it is tailored to meet the specific needs of individual businesses. Business experts help management teams identify barriers to growth, devise and agree a strategy to overcome those barriers and then work with them to execute the plan.

The service has four main areas where it provides help to SMEs:

- commercialising innovation;
- business development;
- access to finance; and
- leadership and management.

In addition to business coaching, GrowthAccelerator fast-tracks clients to trusted providers of business advice. It introduces businesses to networks of investors and connects them with similar businesses on the service.

English SMEs with no more than 250 employees and turnover of up to £40m can apply for the programme.

For further information visit **growthaccelerator.com**.

'WE DON'T RECEIVE WISDOM; WE MUST DISCOVER IT FOR OURSELVES AFTER A JOURNEY THAT NO ONE CAN TAKE FOR US OR SPARE US'

Marcel Proust

GROWTH VOUCHERS PROGRAMME

This government programme helps small businesses get strategic business advice on:

- raising finance and cash flow;
- recruiting and developing staff;
- improving leadership and management skills;
- marketing, attracting and keeping customers; and
- making the most of digital technology.

Businesses are randomly allocated with a Growth Voucher offering a subsidy for up to £2,000 to help cover 50% of the cost of purchasing strategic business advice.

There is more information on this scheme at **gov.uk/apply-growth-vouchers**.

Find support

'GOOD COMPANY IN A JOURNEY MAKES THE WAY SEEM SHORTER'
Izaak Walton

Asset Based Finance Association (ABFA)
The ABFA represents the factoring, ID and ABL industry in the UK and the Republic of Ireland.

abfa.org.uk

British Bankers Association (BBA)
The BBA is the UK's leading association for the banking sector, representing the interests of more than 240 member organisations of all shapes and sizes, including retail banks, wholesale institutions, challenger banks and private banks, with a worldwide presence in 180 countries. **Better Business Finance** is managed by the BBA in collaboration with its business and finance partners. It provides impartial information and support to business and entrepreneurs looking to develop and grow, whether the business is seeking finance, starting out or exporting abroad.

bba.org.uk
betterbusinessfinance.co.uk

British Chambers of Commerce (BCC)
The BCC is an independent business network, with 53 accredited chambers across the UK, representing thousands of businesses of all sizes and sectors, which employ more than five million staff.

britishchambers.org.uk

BVCA
The BVCA is the industry body and public policy advocate for the private equity and venture capital industry in the UK.

bvca.co.uk

CBI
The CBI is the UK's leading business lobbying organisation, providing a voice for employers at a national and international level.

cbi.org.uk

EEF
EEF is the manufacturers' organisation, helping thousands of companies to evolve and compete in a fast-changing world.

eef.org.uk

Federation of Small Businesses (FSB)
The FSB is the UK's largest campaigning pressure group, promoting and protecting the interests of the self-employed and owners of small firms.

fsb.org.uk

Finance & Leasing Association (FLA)
The FLA is the leading trade association for the asset, consumer and motor finance sectors in the UK, and the largest organisation of its kind in Europe. Its members include banks, subsidiaries of banks and building societies, finance arms of leading retail manufacturing companies and a range of independent firms.

fla.org.uk

Forum of Private Business
The forum is a not-for-profit membership organisation, which offers a one-stop-shop business support service, focused on the growth and profitability of small businesses.

fpb.org

GrowthAccelerator
GrowthAccelerator is a unique service led by some of the country's most successful growth specialists and backed by government, where you'll find new connections, new routes to investment and the new ideas and strategy you'll need for your business to achieve its full potential.

growthaccelerator.com

Institute of Credit Management (ICM)
The ICM is Europe's largest credit management organisation, and the second largest globally. The trusted leader in expertise for all credit matters, it represents the profession across trade, consumer and export credit, and all credit-related services. Formed over 70 years ago, it is the only such organisation accredited by Ofqual and it offers a comprehensive range of services and bespoke solutions for the credit professional as well as services and advice for the wider business community, including the acclaimed ICM/BIS Managing Cashflow Guides.

icm.org.uk

Institute of Directors (IoD)
The IoD has been supporting businesses and the people who run them since 1903. As the UK's longest-running organisation for professional leaders, it is dedicated to supporting its members, encouraging entrepreneurial activity and promoting responsible business practice for the benefit of the business community and society as a whole.

iod.com

London Stock Exchange
The London Stock Exchange Group is the largest stock exchange in Europe and the fourth largest in the world. It operates a range of equity and bond markets including AIM, the Main Market and Order Book for Retail Bonds (ORB). It also operates ELITE, a business support and education programme for high-growth private companies.

londonstockexchange.com

Peer-to-Peer Finance Association (P2PFA)
The P2PFA is the industry association representing debt-based alternative finance providers operating through electronic platforms.

p2pfa.info

Quoted Companies Alliance (QCA)
The QCA is the independent membership organisation representing the interests of small- to medium-sized quoted companies.

theqca.com

UK Business Angels Association
The UK Business Angels Association is the national trade association representing angel and early-stage investment in the UK.

ukbusinessangelsassociation.org.uk

UK Crowdfunding Association (UKCFA)
The UKCFA is the largest organisation representing 14 equity crowdfunding businesses in the UK to the public and policymakers, and which has published its own code of practice.

ukcfa.org.uk

The British Business Bank

The British Business Bank is a government-owned financial institution set up to support economic growth by making finance markets work better for small businesses in the UK. It uses funding and guarantees backed by the government to bring more private sector resources into small business lending and investment.

Small firms don't obtain finance directly from the British Business Bank – it makes its impact from generating more activity by the private sector. The Bank is seeking to increase both the level and diversity of funding options available to small businesses in the UK.

With £3.9bn of government funding committed, it aims to leverage in private sector capital to create £10bn of funds for UK businesses over the next 5 years.

WHAT DOES IT DO?

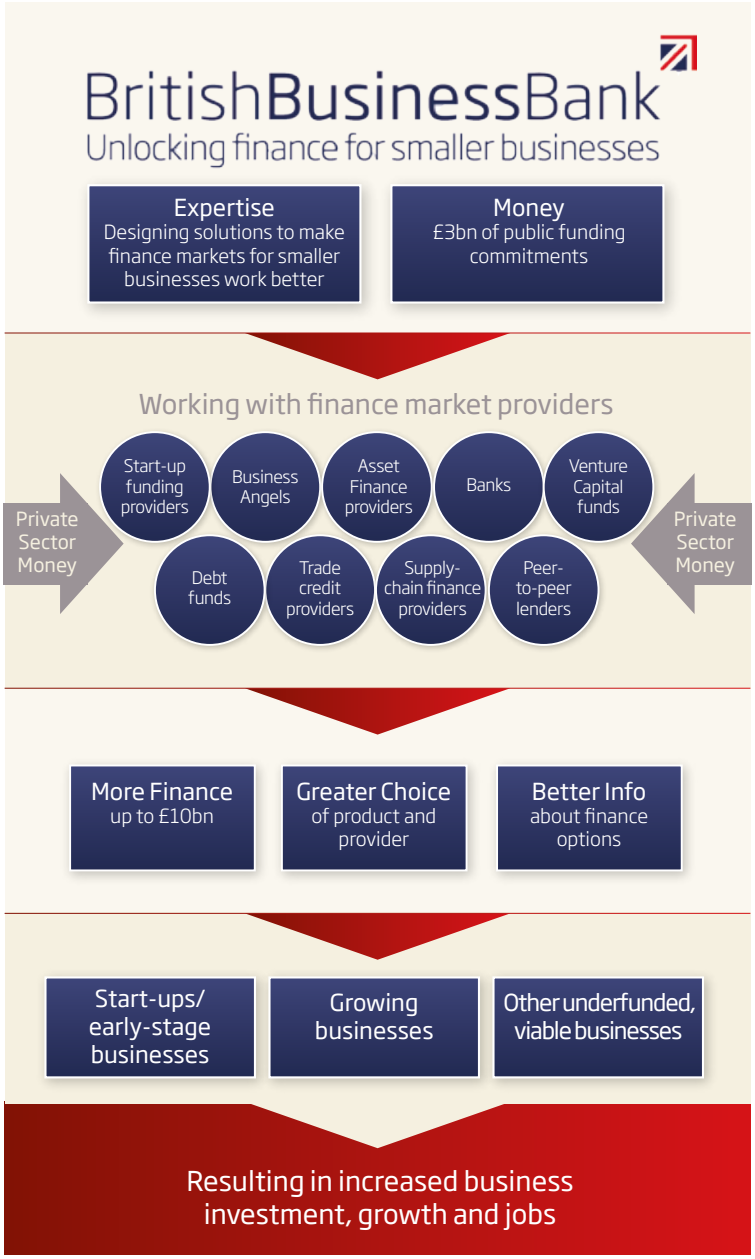
The British Business Bank provides finance and applies guarantees through commercial lenders and investors, who use these financial resources – together with their own money – to lend to or invest in smaller UK firms.

It operates right across finance markets, from supporting early-stage equity funding, through the provision of growth capital, to senior debt for established SMEs, and will share in any returns on investments made. It then recycles these back into further lending and investment.

The solutions it provides to improve finance markets fit into four broad categories.

- **Venture Capital Solutions** – providing funding to the venture capital industry so it invests more in UK businesses (current programmes – Business Angel CoFund, Enterprise Capital Funds).
- **Lending Solutions** – providing funding and guarantees to lenders to encourage more SME lending – in particular to businesses with short track records and low levels of collateral (current programmes – Start-Up Loans, Enterprise Finance Guarantee).
- **Investment Programmes** – supporting and accelerating new lending models in the UK – eg, debt funds, P2P lenders and supply chain finance providers.
- **Wholesale Solutions** – a pilot programme to guarantee bank lending to small firms (first transactions expected autumn 2014).

You can find out more about these solutions and the British Business Bank at **british-business-bank.co.uk**.



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Thanks

We would like to thank the following individuals for their contributions to *The business finance guide.*

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Tim Ward
Chief Executive, QCA

We are also grateful for the support from the various committees within each of the organisations endorsing *The business finance guide.*

THE BRITISH BUSINESS BANK

The British Business Bank aims to ensure that finance markets for small and medium-sized businesses work effectively, allowing such businesses to prosper, grow and build UK economic activity.

The British Business Bank is currently run directly by the Department for Business, Innovation and Skills and is not authorised or regulated by the Financial Conduct Authority or the Prudential Regulation Authority. Once HM Government has received European Commission State aid clearance, which is expected in 2014, this programme will be transferred in its entirety to the British Business Bank plc, which will operate as a government-owned financial institution.

ICAEW CORPORATE FINANCE FACULTY

The faculty's professional network includes more than 70 member organisations and 6,000 members drawn from major professional services groups, specialist advisory firms, companies, banks, private equity, venture capital, law firms, brokers, consultants, policy-makers and academic experts. More than 40% of the membership is from beyond ICAEW.

The faculty is ICAEW's centre of professional excellence in corporate finance. It contributes to policy development and relevant public consultations and provides a wide range of services, events and media to its members, including its magazine *Corporate Financier.*

The faculty launched the first international Corporate Finance qualification (including the 'CF' designation) for practitioners, the Diploma in Corporate Finance, together with the CISI.

ICAEW is a professional membership organisation that promotes, develops and supports over 142,000 chartered accountants worldwide. We provide qualifications and professional development, share our knowledge, insight and technical expertise, and protect the quality and integrity of the accountancy and finance professions.

As leaders in accountancy, finance and business our members have the knowledge, skills and commitment to maintain the highest professional standards and integrity. Together we contribute to the success of individuals, organisations, communities and economies around the world.

Because of us, people can do business with confidence.

ICAEW is a founder member of Chartered Accountants Worldwide and the Global Accounting Alliance.
www.charteredaccountantsworldwide.com
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