

The Keys to Successful Small Business Ownership, Finance and Credit™



Client Curriculum - Personal vs. Business Credit

**Small Business Owner Financial
Education brought to you by:**



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The Keys to Successful Small Business Ownership, Finance and Credit™

National Foundation for Credit Counseling® (NFCC®) - Small Business Owner Counseling Program

Client Workbook

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INTRODUCTION

Welcome! It is our goal you find this material helpful as it was hand selected to address some of the most common challenges faced by the self-employed or small business owners. We aim for this content to complement budget counseling sessions for people like you engaged with a member agency of the National Foundation for Credit Counseling® (NFCC®) across the U.S.

Whether you just started on a self-employment journey, have a business on the side or have dreams of serving millions, you are important to our national economy and local community by creating a job for yourself or others.

It is our hope this program empowers you to make informed decisions about being self-employed and a small business owner by providing you access to a NFCC counselor, information, resources, and tools. As you develop a greater understanding of personal and business finance best practices, you can choose the best course of action to meet your goals.

We would like to thank and acknowledge TD Bank, America's Most Convenient Bank®, and the TD Charitable Foundation, the charitable giving arm of TD Bank, for their support of the NFCC Small Business Owner Financial Counseling and Education Program supporting Small Business Owner Financial Wellness.

Client Overview
Module: 3
Personal vs. Business Credit
Why it Matters

Unable to complete business transactions without credit or compete. Lenders will use a business's credit history when figuring out whether or not to loan the business money. You'll also need credit in order to get business insurance. In many instances, you won't be able to buy goods and services for your business without access to credit.

Personal credit may be only option for a time to finance the business, but you should understand the risks and have a plan to build business credit and increase it to meet the needs of the business. Using personal credit to fund your business can put your family and personal assets at risk. If the business fails or experiences money trouble, creditors will then come after YOU, as you will be personally liable for the expenses incurred by the business.

Business Credit 101

The separation between your personal and your business finances (income and expenses) can be tricky for small businesses, especially when you ARE the business. Experts recommend having a clear distinction between your personal and business finances as far as that's possible. Building business credit aside from your personal credit is part of that equation. In reality, your business and personal credit may remain linked, no matter how hard you work to keep them separate. However, understanding this and how different financial service providers may require both to evaluate your credit worthiness is a positive first step to ensure both personal and business financial wellness.

Your personal credit is connected to you by your Social Security number. Your business credit history ideally is linked to you by your Employer Identification Number (EIN) or Tax ID Number, which is how the government recognizes your business for tax purposes. You can [apply for an EIN online](#) and receive it almost instantly. Technically, if you're a sole proprietor, you don't *need* an EIN for taxes, but to establish business credit, you will.

Your personal credit history is curated by the three major credit bureaus, Equifax, Experian, and Transunion, and you have one profile with each. Experian and Equifax also have business credit reporting services. Your business profile is separate from your personal credit history.

There are credit reporting services that only deal with businesses, with [Dun & Bradstreet](#) being the largest and best known. If you have more than one business, you can have a separate report for each, as long as it has its own EIN.

Personal vs. Business Credit Scores

Your personal credit is frequently summarized into a single number that helps creditors see where you stand at a glance. FICO is the most commonly used method of scoring personal credit. There is no equivalent for businesses; each commercial credit bureau scores and reports its own way.

The most important factors for scoring businesses are usually how you pay your bills, how much debt you carry, and what type of industry you're in. Generally, business credit scores have fewer variables than FICO scores, and it is easier to improve the score for a business than it is for an individual.

On the downside, there are fewer legal protections for business credit. Consumer credit laws allow you to challenge anything on your report and have incorrect negative entries removed. There are no such laws when it comes to commercial credit, which means if there are issues with your business credit report, you could have a much tougher time getting those dealt with. You can challenge discrepancies with the agency that has them listed, but they don't have to respond.

6 Ways to Establish Business Credit

The easiest way to establish business credit is to keep all of the finances separate from the get-go. You can also:

1. **Open a separate business checking account.** Use your business checking account to pay the business's bills and employees, including yourself. If you're incorporated, you *have* to do this, but it's good advice for ALL businesses. Use the EIN we discussed above to identify the account, and use a separate business telephone number, even if it's for a mobile phone.
2. **Apply for and use a business credit card.** Pay business expenses with this card, not with your own personal card. This not only makes tracking expenses much easier, it helps you build credit for the business as you use and pay off the card. If you can't qualify for a business card immediately, start with a secured card, which is backed by money you put in account to guarantee you'll pay.
3. **Ask for credit terms from your vendors.** Even if the credit limit is small to start, and the time frame is relatively short, it will help. Pay the bills on time, and after a few transactions, ask to have the limit and/or term increased. Success with even one or two vendors will give you positive credit references to build on with other business and for possible loans in the future.
4. **Visit with you bank or shop around.** Ask for a credit application and understand what varied financial institutions may look when approving requests as well as the process they use. In addition, establishing or building a relationship you're your existing bank or another will give you an opportunity to seek their advice on the best type of financial product for your business need and it helps to build trust with a key vendor as your business grows or your needs change.
5. **Register with the business credit bureaus** like [Experian](#) and [Equifax](#) and open a business credit file. Apply for a DUNS number from [Dun & Bradstreet](#).
6. **Select your business structure carefully.** The best way to separate your business and personal financial lives is to do it legally. Instead of a sole proprietorship, take yourself out of the mix and form a corporation or LLC. See our article on the [Legal Structure of a Business](#) for the how and whys.

When Personal and Business Credit Mix

There are times your personal and business credit will affect each other, especially if you're a sole proprietor. In most cases, your personal credit will impact your business far more than the other way around.

Many business credit card applications will require your Social Security number. A landlord may want to run a personal credit check before leasing you space. A small business loan likely needs a personal guarantee. In fact, under some circumstances, the Fair Credit Reporting Act does allow lenders to review the personal credit history of sole proprietors for business lending purposes. Credit bureaus don't distinguish between business and personal inquiries, and too many can have a negative impact on your credit score.

For small businesses, your personal and business credit scores can be very closely linked, so it's smart and important to protect both.

*SOURCE: Accion <http://us.accion.org/business-resources/articles-videos/business-credit-vs-personal-credit>

Major Differences Between Business Credit Cards and Personal Credit Cards

We talked about the importance of maintaining separate accounts for personal vs. business income and expenses. When you're setting up shop or taking your business to the next level, you'll probably want to apply for either a small business credit card or a personal credit card to cover company costs. But while these two products have plenty in common, they also have a few notable differences. Here are four you should know about before applying.

1. Small businesses may not be covered by consumer protections.

You may think of yourself as a consumer, especially after you hang up the "closed" sign on your small business's door every evening. But consumer protection laws, such as the Credit CARD Act of 2009, generally don't apply to your business. Potentially, your APR could change overnight, or you could be charged exorbitant late fees for small infractions.

Because most issuers extend consumer protections as a courtesy to small businesses, you probably won't have to worry too much about this – but it's a good thing to keep in mind, since those protections aren't available in every case. If your issuer is among the few that does not extend these protections, or doesn't clearly express a position in the terms and conditions, ask about what you should expect.

2. Business credit cards affect business credit (and sometimes personal credit, too).

For most small business owners, the line between personal and business credit is blurry. If you sign a personal guarantee for your business credit cards, as almost all require, you're liable for the company's debt should your business miss payments. Several issuers also weigh your personal credit score heavily when deciding how much credit to extend to you. It's not surprising that the reporting, too, is a mixed bag.

Many small business credit card issuers report business activity to both consumer and commercial credit bureaus. Others just report to commercial credit bureaus, but may report to consumer bureaus in certain cases (for instance, if your company falls behind on payments). If your business credit activity is reported to consumer credit bureaus, it's generally included on your credit reports and factored into your FICO scores, just as consumer activity would be. If you're not sure how your credit card reports, call your issuer to find out.

3. Understand your need for credit and shop around for best card or financial product.

If you're making a lot of expensive purchases, a credit card with rewards may be the best choice or if you are confident you will pay off the balance quickly perhaps some credit cards may offer appealing incentives such as mileage that could benefit you personally or the business. Some business credit cards offer bonus rewards on phone bills, Wi-Fi or office supplies, a boon for companies spending heavily in these areas. However, this may not be as helpful if you're a sole proprietor and tend to use office supplies sparingly. If you're having a hard time finding a business credit card that matches your needs, you may be better off with a flat-rate rewards program that lets you earn bonuses on all your purchases, or a personal credit card.

Business credit scores from Equifax and Experian (but not Dun & Bradstreet) use your credit utilization to calculate your business credit score, so a higher limit can make it easier to use less of your available credit and improve your standing.

Note that if you use a personal credit card, you'll have to use it only for business expenses and pay with it only with business money if your company's a limited liability company, S-corporation or C-corporation. If you commingle expenses in this case, you may lose your personal liability protection. But even if you're a sole proprietor, it's easier to separate expenses so you can identify deductions more easily during tax season.

Which card should you get?

If you're still on the fence, here are some guidelines to consider.

A business credit card may be better for:

- An entrepreneur who wants to establish business credit for his or her business.
- A company with major business expenses that align with most business credit card reward categories.
- Someone looking for a higher credit limit for his or her business.

A personal credit card may be better for:

- A sole proprietor with minimal overhead costs.
- Someone whose spending doesn't align with business credit card spending categories.
- Someone who doesn't anticipate applying for a small business loan anytime soon and isn't interested in building business credit.
- The sooner you find a credit card that fits your business's needs, the sooner you'll be on your way to better rewards and improved terms.

*SOURCE: <https://www.nerdwallet.com/blog/credit-cards/major-differences-business-credit-cards-personal-credit-cards/>

Alternative Online Loan Basics

Because it can be difficult to qualify for bank loans, a new generation of online, alternative lenders are stepping up to get business owners capital. These aren't your grandparent's loans. These lenders offer loans that are basically the same as bank loans, but the rates tend to be higher, while the credit score criteria is more lax. Typically, these loans are for 1 – 5 years and come with a fixed monthly payment. Online term loans can be used for virtually any business need.

What You Need to Know About Online Business Loans

Pros:	Cons:
Reasonable interest rates (7 – 30%)	Higher interest rates than bank loans
Quick turnaround time (compared to banks)	Little or no mentorship
Less effort and documentation needed	May have pre-payment penalty
Fixed, predictable monthly payments	Requires good personal and business credit
Helps improve business credit score	Available for many uses
May require collateral	Available for many uses
Typically, must have 2 years in business	

Best Uses for Online Loans:

- Working capital
- Purchasing inventory
- Purchasing equipment
- Refinancing
- Acquiring other businesses

If you're unable to qualify for a bank loan or simply need a faster turnaround time, online lenders are a great option. Applying usually takes less than 2 hours—and you can do it from the comfort of home. The rates are a little higher than bank loans, but the convenience can't be beat. By making timely payments, these loans can also help you build your business credit rating.

Source: <https://www.nav.com/business-financing-options/online-loans/>

Client Worksheet:

Thinking about your goals and future, what steps can you take to better manage your business?

GOALS	I've Done It	Will Do 1 to 3 mos.	I Will think about it
Follow thru on my goals to reduce existing credit card debt			
Improve my credit score to prepare for future needs and business credit			
Establish a business savings account to fund growth or emergencies			
Get a mentor to help me create a plan to grow my business without sacrificing my personal assets			

RESOURCES & HELPFUL LINKS

Alternative and Online Lenders

<https://www.nerdwallet.com/blog/loans/what-is-an-online-loan/>

<https://us.accion.org/resource/alternative-lending-landscape/>

Assessing Your Business' Financial Needs

<http://virtual-advisor.org/td/assessingcompanyfinancialneeds/>

Business Advising

www.businessadvising.org

Business Borrowing 101

<http://www.venturize.org/borrowing-101/>

Business Borrowers Bill of Rights

<http://www.responsiblebusinesslending.org/>

Business Loan Checklist

<http://www.venturize.org/get-started/loan-app-checklist/>

Business Loans for Poor Credit Score

<https://loans.usnews.com/business-loans-for-bad-credit>

Cash flow

http://www.score.org/60_guide_managing_cash_flow.html

Cash flow management as part of the SBA's financial management series

http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_capgrowth.doc

Community Development Financial Institutions/Mission Driven Lenders and Education Resources

<http://www.venturize.org/mission-driven-lenders-locator-map/>

Marketplace Lenders

<http://www.venturize.org/borrowing-101/types-of-lenders/online-only-marketplace-lenders/>

Mentoring, Resources and Tools for Small Business Owners

www.score.org

National Association of Latino Community Asset Builders

<https://www.nalcab.org/>

National Black Chamber of Commerce

<http://www.nationalbcc.org/>

RESOURCES & HELPFUL LINKS

Small Business Administration Resources and SBA Loans

<https://www.sba.gov/>

SBA Loans

<https://www.sba.gov/loans-grants/see-what-sba-offers/sba-loan-programs>

Women's Business Centers

<https://www.sba.gov/tools/local-assistance/wbc>

About the NFCC®

Founded in 1951, the National Foundation for Credit Counseling® (NFCC®) is the nation's first and largest nonprofit dedicated to improving people's financial well-being. With offices serving 50 states and Puerto Rico, NFCC Certified Credit Counselors are financial advocates, empowering millions of consumers to take charge of their finances and their futures.

NFCC member agencies assist individuals and families regardless of income or circumstances to ensure they never have to face their challenges alone. NFCC Certified Credit Counselors nationwide are trained, certified and ready to complete a comprehensive financial review and action plan to help clients meet their financial goals—in person, over the phone or online.

NFCC member agencies provide affordable, one-on-one, customized financial reviews and actions plans to address:

- Credit card debt
- Student loan debt
- Debt management
- Prepurchase housing decisions
- Foreclosure prevention
- Bankruptcy
- Overall money management
- Financial education needs
- Asset building
- Small business owner finances

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