

Trading Up

No cash? No problem. Here's how smart entrepreneurs use barter to help save money, create connections and grow their businesses.

By Mark Henricks | [Entrepreneur's StartUps](#) - [February 2005](#)

When Rich Kazimir was getting his IT services firm off the ground in early 2004, the former engineer knew he and his staff needed sales training, but he didn't have much cash to pay for it. The solution? The 47-year-old entrepreneur offered to swap services with a local business coach.

The trainer coached him on business development and helped him set up a sales management plan for the business development manager of his [CMIT Solutions](#) franchise in Flemington, New Jersey. In return, Kazimir got the trainer online. No cash changed hands. Instead, both parties contributed what they could, and got what they wanted. "We built her a nice website," Kazimir says, "and she provided me with marketing and sales coaching."

Barter Background

Barter--the cash-free exchange of goods and services--is a huge and long-established activity for businesses old and new, large and small. The International Reciprocal Trade Association (IRTA), a nonprofit organization of commercial and corporate barter exchanges based in Rochester, New York, estimated in 2001 that \$7.5 billion in sales flows through commercial barter channels each year. The IRTA also estimated that figure was growing at 8 percent a year, and that 300,000 companies, including startups and Fortune 500 firms, would participate in trading exchanges in 2002.

The numbers reported by barter exchanges are minuscule, however, compared with the amount of barter that occurs directly between firms, as in the case of Kazimir and the sales trainer. No one tracks direct barter, so no one knows how big it is. But, says Tom McDowell, executive director of the National Association of Trade Exchanges (NATE) in Mentor, Ohio, "The amount of direct barter dwarfs what we do on an organized basis."

Experts estimate that millions of companies, especially young ones, employ barter as a regular or occasional business tool. Barter provides one important benefit: helping companies dispose of excess inventory by trading it for valuable goods or services, notes Phyllis Malitz, a CPA and barter expert in Wilmette, Illinois. That can be especially useful for startups whose markets aren't developed enough to consume all their capacity.

At the same time, barter helps startups conserve cash because they don't have to lay out precious, hard-earned dollars for necessary goods and services. "Paying for business expenses with trade dollars leaves more cash available for the payment of strictly cash expenses," notes Malitz.

Barter also has some unexpected advantages. You may be able to fend off a creditor by offering excess inventory as partial or full payment for a debt. Likewise, if someone owes you money and

you're having trouble collecting it, you may be able to barter part of the debt for useful services or products in lieu of cash.

Startups using barter report that it's an exceptionally powerful marketing tool. "One of the biggest benefits I've seen is referrals," says Mark Patrick Collins, 32, owner of [Sign A Rama](#) in Skokie, Illinois. The former aviation-industry employee, who started running his sign business in 2003, says trades for computers, networking services and even a condominium for him to live in have also helped the six-employee company's nonbarter sales: "The businesses you barter with refer you to other customers who will do cash business."

But barter isn't better in every way. One frequent complaint is that businesses with something to trade can't quickly find a barter partner for a specific product or service. "That is a disadvantage," acknowledges Joan Varner, co-owner of [Illinois Trade Association](#), a barter exchange in Niles, Illinois. "You may have to be willing to wait."

Contrary to popular belief, barter carries no inherent tax advantages. The IRS regards barter exchanges as the same as cash deals, says IRTA executive director Krista Vardabash. "It's taxed just like income," says Vardabash. "One barter dollar is equal to one U.S. dollar."

Commercial barter exchanges work closely with the IRS. Members of such exchanges receive 1099 forms at the end of the year to report their barter transactions, so the appropriate taxes can be levied. With direct barter, it's different. Although taxes are due on direct trades, collecting them is another matter. "[The IRS] knows they can't control that," says Vardabash, who works closely with the IRS on policing exchange barter.

Barter isn't for every company, either. Hospitality and media goods and services are the biggest categories of commercial barter. Items such as unoccupied hotel rooms and unpromised radio airtime are ideal barter goods, because they're highly perishable--if no one uses them, they're wasted. So if you either provide or consume travel, entertainment, advertising or similar goods and services, you're a good candidate for barter. "The businesses that do best in barter are retail, service and professional--anybody with a disposable commodity that has no shelf life," says McDowell.

Many other goods and services, from carpet cleaning to new automobiles, are actively traded on exchanges and between direct-barter customers. If, however, you provide only one specialized product, such as a part used in one machine made by one manufacturer, you're not a good candidate for barter, since you won't find many--or any--takers for what you are offering. The same goes for highly specialized services.

Barter How-To

If you're interested in barter, you must first decide whether to try direct barter or a barter exchange. Experts like Malitz recommend exchanges for their convenience and flexibility. These networks act as brokers connecting hundreds or thousands of businesses in a system that allows them to exchange their offerings for barter dollars, which can in turn be swapped for goods and services offered by other members. The exchange adds value by assigning you a barter broker

who can help you locate the barter products and services you need. In addition, the exchange keeps track of the paperwork, collects fees on the transactions to all parties and reports to taxing authorities.

Direct exchanges sound comparatively simple--you scratch another business owner's back, and he or she scratches yours. No paperwork or fees are involved and, in the vast majority of cases, taxes are not paid. No wonder direct barter is overwhelmingly more common than commercial barter. It does have its challenges, however.

The first is finding someone who has what you want, wants what you have and is willing to barter for it. Vivien Teo, a 28-year-old partner in New York City startup [Vroom Media Group LLC](#), ran into a lot of skepticism and blind alleys when she looked for chances to barter her PR and brand marketing firm's services. "When we tried approaching some businesses about bartering, they were not very excited about it," she says. Teo kept at it and eventually found suppliers willing to barter for photography, and web and logo design. She even found a spa that would swap PR work for free treatments, which Teo has used both to pamper herself and to reward clients.

Even if it takes a while to find a willing trader, don't be too quick to jump into the deal. The second challenge of direct barter is not letting others take advantage of you. You don't want to trade your goods or services for something of lesser value. Knowing your own margins is essential to bartering effectively, Vardabash says. Knowing your barter partner is equally critical.

Kazimir says he was only comfortable with his website-for-training swap because he took the time to get to know his prospective barter partner. The two held hour-long, semiweekly meetings for two months to discuss what their expectations were and how they would price their respective contributions. "I'd recommend bartering with someone you know," Kazimir concludes. "And I'd look for something, like references, that makes you feel you're dealing with somebody trustworthy."

There are some things smart barterers don't do. One is converting a cash customer to a barter customer. "A trade exchange never takes away a cash customer," McDowell says. Barter is for excess capacity and unused inventory, experts stress. If you're doing more than 5 percent of your sales volume in barter, according to accepted barter wisdom, you may be abusing the technique. "It's great for extra business, but it can't be the only business you have," McDowell warns.

In direct barter, you can, however, convert barter customers to part-cash, part-trade. That's something Collins has done, so far without complaint, with his formerly pure-barter customers. "In the beginning, a couple of sales were 100 percent trade," he says. "I found I can't do [that]. I have to pay materials and labor costs in cash, and my overhead is all in cash, too."

Nor can you expect to pay all your suppliers in barter. Barter is good for many kinds of expenses, from coffee services and window cleaners to incentive travel and restaurant meals. But you can't refill your inventory with barter, and you can't pay your utilities, taxes or, most likely, your rent. "There are tons of things you can do with barter," says Malitz, "but it's not going to be for your core expenses."

Experienced barterers generally agree with these warnings, but if there's one universal bit of advice about barter, it's that creativity and innovation are rewarded more than naysaying and excessive caution. Edward Posherstnik, owner of 3-year-old printer [IBG Creative Services](#), says barter--especially referral business--has been key in expanding his company, and he has approached it creatively. He has obtained design services in exchange for the chance to post ads or place business cards and brochures on his company's website or in its Old Bridge, New Jersey, office. He also lets a local art teacher hold lessons in the IBG offices. "Since she is also skilled in marketing techniques, she provides research and marketing services to our company [in return]," says Posherstnik, 45. "We are not limited to anything. IBG Creative Services is willing to consider any barter offer."

Barter's Future

The future for barter is unclear. While the trend-trackers at the IRTA report that barter is growing strongly in terms of exchanges, members and volume, the NATE's 2004 report showed a much smaller amount of business flowing through barter than past reports have shown. McDowell says this is mostly because the NATE got more accurate information about franchise barter exchanges that revealed they weren't doing as much volume as expected.

McDowell adds, however, that the growth of online auction services such as eBay has hurt barter by giving companies an easier way to turn excess inventory into cash. Attempts to harness the internet for barter by setting up online barter exchanges have been universally unsuccessful, he says, despite a number of well-financed efforts.

Meanwhile, barter remains a well-established practice that startups find especially useful. "It worked out really well," Kazimir says of his foray into direct barter. "We built [our barter partner] a nice site that she's very happy with, and I'm pleased with the training and plan that I got from her. It's been win-win."

The Swap Team

Ready to engage in organized barter? You have several hundred commercial exchanges to choose from. Local exchanges should probably be the first choice for most startups, because new companies usually have a greater need for local services and goods, says Krista Vardabash, executive director of the International Reciprocal Trade Association (IRTA). You can find online directories of barter exchanges at the [IRTA's](#) website, as well as at the site of the [National Association of Trade Exchanges](#) (NATE).

Look for an exchange whose membership includes companies that supply products and services you need, and that are likely to be customers for your offerings. Costs are also something to consider. Most exchanges charge \$300 to \$700 to join, plus a 10 to 15 percent fee on each transaction and a monthly membership fee of \$20 to \$30, says Tom McDowell, NATE's executive director. Check for a guarantee that refunds your initial membership fee if you don't get value out of the exchange within a few months.

Given the costs, it makes sense to do due diligence on your prospective exchange. Talk to other members. Run a credit report on the exchange. Not all exchanges are run equally well. Some exchange owners skim off the most desirable barterers for their own use, or issue so much barter credit that the exchange collapses. "Check out who you're doing business with," urges McDowell, "just as if it were a cash customer."

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