

## ***Guideline for Preparing A Business Plan***

*NOTE: While researching and before taking your business plan to a loan officer, contact the Bessemer Business Center for a final review of the plan. This will help ensure that your plan is complete, which may save you time and money.*

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*NOTE: Sections of this business plan outline were adapted from a business plan outline prepared by the SBDC at Jacksonville State University.*

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***Reading the entire text of this document is the first step in preparing your business plan.***

There are two basic reasons for preparing an extensive business plan. First, it requires the entrepreneur to thoroughly investigate the factors that will have a bearing on the success of the business. Second, it will enhance the ability of the entrepreneur to secure financing by providing an organized overview of the venture for lenders and investors. It also provides insight into the entrepreneur's ability to define and develop strategies for critical areas of the business. The following outline has been prepared to help the entrepreneur assemble the facts that are essential to good business planning. Complete your business plan using the accompanying outline to ensure that the necessary details are included. Keep in mind that thoroughness, clarity and rationality of the plan are all factors that will play key roles in successfully financing, starting and operating your business.

Because these guidelines were written to cover a variety of possible businesses, rigid adherence to them is not possible or even desirable for all businesses. Not all parts of all sections will be necessary for each individual's business plan.

## ***I. The Industry, the Company and its Products***

The purpose of this section is to assist you in describing your business venture in a detailed but succinct manner. You must clearly present the business you are in, the product you will offer and the nature of your industry.

### **A. THE INDUSTRY**

Present the status and prospects for the industry in which the business will operate. Discuss new products and developments, new markets and customers, and any other trends that could affect the business. Identify all sources of information used to describe these trends.

### **B. THE COMPANY**

Briefly describe what business area your company is in, or intends to enter, what products or services it will offer, and who are or will be its principal customers. Also, discuss the ownership and legal form of the company. Consult your attorney for which form of corporation, partnership or sole proprietorship is best for you.

### **C. THE PRODUCTS OR SERVICES**

1. Describe in detail the products or services to be sold, as well as the application of your product or service. Emphasize any unique features of your product or service and highlight differences between what is currently on the market and what you will offer. Define the current state of development of the product or service; include a photograph, if

applicable.

2. Proprietary Position: Describe patents, trade secrets, or other proprietary features. Discuss any head start that you might have that would enable you to achieve a favorable position in your industry.

## ***II. Market Research and Analysis***

The purpose of this section is to present enough facts to learn if your product or service has a substantial market in a growing industry and can achieve sales despite a competitive market. This section is one of the most difficult to prepare and one of the most important. Almost all subsequent sections of the business plan depend on sales estimates developed in this section. The sales levels you project, based on market research and analysis, directly influence the size of the operation, the marketing plan, and the amount of debt and equity capital required.

Because of the importance of market analysis and the dependence of other parts of the plan on the sales projections, you may want to prepare this section of the business plan before you do any other. Allow enough time to do this section thoroughly and check alternate sources of market data.

### **A. CUSTOMERS**

Discuss who your customers are for the product or service. Who and where are the major purchasers? What is the basis for their purchase decision: price, quality, service, personal contact or some combination of these factors?

### **B. MARKET SIZE AND TRENDS**

Describe the primary market for your product, both geographically and in terms of total sales volume. Also, describe the seasonal fluctuations and the potential annual growth of the total market for your product or service, and discuss the major factors affecting that growth (industry trends, economic trends, government policy, population shifts).

### **C. COMPETITION**

Make a realistic assessment of the strengths and weaknesses of competitive products and services and name the companies that supply them. Compare these competing products or services by price, performance, service, warranties, and other pertinent features. Present a short discussion of the current advantages of competing products and services and state why they are not meeting customer needs.

### **D. MARKET SHARE AND SALES**

Summarize what it is about your product or service that will make it saleable in the face of current and potential competition. Identify major customers who are willing to make purchase commitments and if possible attach their commitment letters to your plan. Discuss which customers would be major purchasers in the future and why. Based upon your assessment of the advantages of your product or service, market size and trends, customers, the competition and their product,

and the sales trend in prior year, estimate your share of the market and your sales in units and dollars for the next two years. Be sure to state any assumptions upon which your projections are based.

### ***III. Marketing Plan***

#### **A. OVERALL MARKET STRATEGY**

Describe the general marketing philosophy and strategy of the company. This should be derived from marketing research and evaluation. It should include a discussion of what kinds of customer groups will be targeted for initial intensive sales promotions as well as which groups will be targeted for later sales efforts.

#### **B. PRICING**

The pricing policy is one of the most important decisions you will have to make. The price must be right to penetrate the market, maintain a market position, and produce profits. Discuss prices to be charged for your product or service, and compare your pricing policy with that of your major competitors.

#### **C. SALES TACTICS**

Describe the methods that will be used to make sales and distribute the product or service. Will the company use its own sales force, independent sales representatives, or distributors? Discuss the margins to be given to retailers, wholesalers, and salesmen and compare them to those of your competition.

#### **D. ADVERTISING AND PROMOTION**

Describe approaches the company will use to bring its product to the attention of prospective purchasers. The schedule and cost for advertising and promotion should be presented. If advertising and promotion will be significant expense item, an exhibit of how and when these costs will be incurred should be included.

### ***IV. Operating Plan***

The operating plan should describe facilities, location, space requirements, capital equipment and labor force that is required to provide the company's product or service.

The discussion guidelines given below are general enough to cover different businesses. Only those that are relevant to your particular business should be addressed in your business plan.

#### **A. LOCATION**

Describe the planned location of the business and discuss the advantages and disadvantages of the site in terms of wage rates; labor availability; proximity to customers and suppliers; access to wholesalers, distributors and transportation; state and local taxes and laws; utilities; and zoning.

#### **B. FACILITIES AND IMPROVEMENTS**

If yours is an existing business, describe the facilities currently used. If your firm is new, describe how and when the facilities to start business will be acquired. Discuss how and when space and equipment will be expanded to the capacity required for future sales projections. Discuss any plans to add to or improve

existing space. Explain future equipment needs and indicate the cost and timing of such acquisitions.

C. **STRATEGY AND PLANS**

Describe the process involved in production of your product or service. Also, present a plan that shows cost-volume information at various sales levels of operation with a breakdown of material, labor, purchased components, and overhead. Manufacturers should briefly describe their approach to quality control, production and inventory control. Explain the quality control and inspection procedures the company will use to minimize service problems and ensure customer satisfaction.

D. **LABOR FORCE**

Exclusive of management functions, does the local force have the necessary skills, in sufficient quantity and quality, to produce the product? If their skills are inadequate, describe the training that you would use to upgrade them.

## ***V. Management Team***

The management team is the key to turning a good idea into a successful business. Bankers and investors look for a committed management team with a balance of technical, managerial, and business skills. The proposal should include a description of the organizational structure, key management personnel and their primary duties, and the board of directors, if applicable.

A. **ORGANIZATION**

In a table, present the key management roles in the company and the individual who will fill each position. Discuss any current or past situations where the management personnel have worked together, and indicate how their skills complement each other and result in an effective management team.

B. **KEY PERSONNEL**

Describe the exact duties and responsibilities of each key member of the management team. For each individual, include a brief statement of career highlights that focuses on his or her ability to perform the assigned role. A complete resume for each member should be included as an exhibit to the business plan.

C. **MANAGEMENT COMPENSATION AND OWNERSHIP**

State the salary that is to be paid to each member. Set forth stock ownership planned for key personnel, the amount of their equity investment, and any performance-dependent stock options or bonus plans that are contemplated.

D. **BOARD OF DIRECTORS**

Discuss the company's philosophy as to the size and composition of a board of directors. Identify proposed board members and include a short statement about each member's background.

## ***VI. The Financial Plan***

The financial plan is basic to the evaluation of a business opportunity and should represent your best estimate of future operations. It can also serve as an operating plan for your management team.

In developing a financial plan, several basic forecasts must be prepared. Many decisions will be based on what you present here. At the appropriate time, your advisors may recommend some changes, but it is vitally important that you apply your best efforts in formulating these forecasts.

- A.     **SOURCES AND USES OF FUNDS**  
        Please refer to Exhibit VI-A.
- B.     **PRO FORMA CASH FLOW ANALYSIS**  
        Please refer to Exhibit VI-B.
- C.     **PROFIT AND LOSS FORECASTS**  
        Please refer to Exhibit VI-C.
- D.     **PRO FORMA BALANCE SHEETS**  
        Please refer to Exhibit VI-D.

For an existing business, balance sheets and income statement for the current and previous three years should be provided. After you have completed preparation of the financial exhibits, briefly highlight the important conclusions that can be drawn. Finally, explain all of your assumptions and the sources of your data. If you need additional assistance in preparing this section, you should also refer to Section IX entitled "Developing Cash Flow, Balance Sheet and Income Statement Pro Formas."

## ***VII. Executive Summary (Primarily for Loan Purposes)***

Once you have completed the basic business plan it will be necessary to provide a brief overview of the plan. This summary is a necessity as lenders do not want to read through an entire plan, initially, to find out what you want or expect. They will, at first, simply want to see to minimum of information in order to qualify you for a loan.

The summary should be completed only after all areas of the business plan are completed. Then, place the executive summary at the very beginning of your plan.

The following information should be included:

- A.     **COVER LETTER**
  - 1.     Company name and type
  - 2.     Dollar amount requested
  - 3.     Terms and timing
  - 4.     Application of funds
  - 5.     Plan for repayment

- B. SUMMARY OF LOAN APPLICATION
  - 1. Business description and history
  - 2. Location and description of facility
  - 3. Product/Service
  - 4. Legal structure (sole proprietorship, partnership, Sub S corporation, C corporation, Limited Liability Company)
  - 5. Market and competition
  - 6. Management expertise
  - 7. Owners' personal financial statements

### ***VIII. Appendix (Supporting Data)***

Additional information backing up or supporting your loan request may be needed. The following are examples of the type of information which may be useful.

- A. LETTERS OF INTENT
- B. CUSTOMER CONTRACTS OR PURCHASE ORDERS
- C. LAYOUT OF EXISTING OR PROPOSED BUSINESS FACILITY
- D. CHARACTER AND BUSINESS REFERENCES
- E. OWNERS' INDIVIDUAL TAX RETURNS
- F. SET OF DRAWINGS OF PRODUCT (MANUFACTURER)
- G. COPY OF ARTICLES OF INCORPORATION (IF APPLICABLE)
- H. APPRAISAL REPORTS
- I. COPY OF LEASE AGREEMENT (IF APPLICABLE)
- J. COPY OF PATENT, COPYRIGHT, ROYALTY AGREEMENT, FRANCHISE AGREEMENT, ETC.
- K. ANY INFORMATION REQUIRED TO SUPPORT THE MAJOR POINTS IN THE BUSINESS PLAN
- L. SURVEYS
- M. DEMOGRAPHICS
- N. NEWSPAPER AND MAGAZINE CLIPPINGS
- O. SPECIAL AWARDS AND RECOGNITION



## ***Exhibit VI-A: Sources and Uses of Funds***

### ***Funds available:***

<i>Owners' funds</i>	\$ _____	
<i>Other equity</i>	\$ _____	
<i>Loan No. 1</i>	\$ _____	
<i>Loan No. 2</i>	\$ _____	
<i>Total</i>		\$ _____

### ***Uses of funds:***

<i>Land</i>	\$ _____	
<i>Building</i>	\$ _____	
<i>Equipment</i>	\$ _____	
<i>Machinery</i>	\$ _____	
<i>Renovations</i>	\$ _____	
<i>Prepaid insurance</i>	\$ _____	
<i>Promotions</i>	\$ _____	
<i>Inventory</i>	\$ _____	
<i>Furniture &amp; fixtures</i>	\$ _____	
<i>Deposits</i>	\$ _____	
<i>Other</i>	\$ _____	
<i>Total</i>		\$ _____

### ***CASH BALANCE:***

*(or working capital)* \$ \_\_\_\_\_

***Exhibit VI-E: Capital Equipment List***  
 (To be purchased with proceeds of the loan)

<u>MAJOR EQUIPMENT AND ACCESSORIES</u>	<u>MODEL</u>	<u>COST OR LIST PRICE</u>
_____	_____	\$ _____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
	<b>TOTAL:</b>	\$ _____
<u>MINOR EQUIPMENT</u>		
_____	_____	\$ _____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
	<b>TOTAL:</b>	\$ _____
<u>OTHER EQUIPMENT</u>		
_____	_____	\$ _____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
	<b>TOTAL:</b>	\$ _____
	<b>GRAND TOTAL:</b>	\$ _____

## ***Exhibit VI-B: Pro Forma Cash Flow Analysis***

<b><u>Month:</u></b>	<b><u>1</u></b>	<b><u>2</u></b>	<b><u>3</u></b>	<b><u>4</u></b>	<b><u>5</u></b>	<b><u>6</u></b>
<b>Sales:</b>						
Sales No.1	_____	_____	_____	_____	_____	_____
Sales No.2	_____	_____	_____	_____	_____	_____
Less returns	_____	_____	_____	_____	_____	_____
<b>TOTAL SALES</b>	_____	_____	_____	_____	_____	_____
<b>Total</b>						
<b>Acc'ts Receivable:</b>	_____	_____	_____	_____	_____	_____
<b>Disbursements:</b>						
Material cost	_____	_____	_____	_____	_____	_____
Labor	_____	_____	_____	_____	_____	_____
Management	_____	_____	_____	_____	_____	_____
Payroll tax	_____	_____	_____	_____	_____	_____
Benefits	_____	_____	_____	_____	_____	_____
Advertising	_____	_____	_____	_____	_____	_____
Auto Expense	_____	_____	_____	_____	_____	_____
Contributions	_____	_____	_____	_____	_____	_____
Charge Costs	_____	_____	_____	_____	_____	_____
Dues	_____	_____	_____	_____	_____	_____
Freight	_____	_____	_____	_____	_____	_____
Insurance	_____	_____	_____	_____	_____	_____
Legal/acct.	_____	_____	_____	_____	_____	_____
Office Supplies	_____	_____	_____	_____	_____	_____
Shop supplies	_____	_____	_____	_____	_____	_____
Travel	_____	_____	_____	_____	_____	_____
Telephone	_____	_____	_____	_____	_____	_____
Utilities	_____	_____	_____	_____	_____	_____
Repairs	_____	_____	_____	_____	_____	_____
Tax/license	_____	_____	_____	_____	_____	_____
Rent/lease	_____	_____	_____	_____	_____	_____
Other expense	_____	_____	_____	_____	_____	_____
Principal pmt.	_____	_____	_____	_____	_____	_____
Interest pmt.	_____	_____	_____	_____	_____	_____
Add. inventory	_____	_____	_____	_____	_____	_____
Equipment	_____	_____	_____	_____	_____	_____
Fixtures	_____	_____	_____	_____	_____	_____
Other Assets	_____	_____	_____	_____	_____	_____
Income taxes	_____	_____	_____	_____	_____	_____
<b>Total</b>	_____	_____	_____	_____	_____	_____
<b>NET CASH FLOW</b>	_____	_____	_____	_____	_____	_____
Plus: Working cap. at the begin. of the month	_____	_____	_____	_____	_____	_____
<b>CUMULATIVE</b>	_____	_____	_____	_____	_____	_____

<b><u>Month:</u></b>	<b><u>7</u></b>	<b><u>8</u></b>	<b><u>9</u></b>	<b><u>10</u></b>	<b><u>11</u></b>	<b><u>12</u></b>
<b>Sales:</b>						
Sales No.1	_____	_____	_____	_____	_____	_____
Sales No.2	_____	_____	_____	_____	_____	_____
Less returns	_____	_____	_____	_____	_____	_____
<b>TOTAL SALES</b>	_____	_____	_____	_____	_____	_____
<b>Total</b>						
<b>Acc'ts Receivable:</b>	_____	_____	_____	_____	_____	_____
<b>Disbursements:</b>						
Material cost	_____	_____	_____	_____	_____	_____
Labor	_____	_____	_____	_____	_____	_____
Management	_____	_____	_____	_____	_____	_____
Payroll tax	_____	_____	_____	_____	_____	_____
Benefits	_____	_____	_____	_____	_____	_____
Advertising	_____	_____	_____	_____	_____	_____
Auto Expense	_____	_____	_____	_____	_____	_____
Contributions	_____	_____	_____	_____	_____	_____
Charge Costs	_____	_____	_____	_____	_____	_____
Dues	_____	_____	_____	_____	_____	_____
Freight	_____	_____	_____	_____	_____	_____
Insurance	_____	_____	_____	_____	_____	_____
Legal/acct.	_____	_____	_____	_____	_____	_____
Office Supplies	_____	_____	_____	_____	_____	_____
Shop supplies	_____	_____	_____	_____	_____	_____
Travel	_____	_____	_____	_____	_____	_____
Telephone	_____	_____	_____	_____	_____	_____
Utilities	_____	_____	_____	_____	_____	_____
Repairs	_____	_____	_____	_____	_____	_____
Tax/license	_____	_____	_____	_____	_____	_____
Rent/lease	_____	_____	_____	_____	_____	_____
Other expense	_____	_____	_____	_____	_____	_____
Principal pmt.	_____	_____	_____	_____	_____	_____
Interest pmt.	_____	_____	_____	_____	_____	_____
Add. inventory	_____	_____	_____	_____	_____	_____
Equipment	_____	_____	_____	_____	_____	_____
Fixtures	_____	_____	_____	_____	_____	_____
Other Assets	_____	_____	_____	_____	_____	_____
Income taxes	_____	_____	_____	_____	_____	_____
<b>Total</b>	_____	_____	_____	_____	_____	_____
<b>NET CASH FLOW</b>	_____	_____	_____	_____	_____	_____
Plus: Working cap. at the begin. of the month	_____	_____	_____	_____	_____	_____
<b>CUMULATIVE</b>	_____	_____	_____	_____	_____	_____

## ***Exhibit VI-C: Profit and Loss Forecast***

	<u>Year 1</u>		<u>Year 2</u>	
	<u>Amount</u>	<u>% of Net</u>	<u>Amount</u>	<u>% of Net</u>
<b>Sales:</b>				
Sales No.1	_____	_____	_____	_____
Sales No.2	_____	_____	_____	_____
Gross Sales	_____	_____	_____	_____
Less Returns	_____	_____	_____	_____
<b>NET SALES:</b>	_____	<u>100%</u>	_____	<u>100%</u>
Cost of goods sold:	_____	_____	_____	_____
Beginning Inventory	_____	_____	_____	_____
Purchases	_____	_____	_____	_____
Additional Inventory	_____	_____	_____	_____
Goods Available	_____	_____	_____	_____
Less Ending Inventory	_____	_____	_____	_____
<b>Total material cost</b>	_____	_____	_____	_____
<b>G &amp; A Expenses:</b>				
Labor	_____	_____	_____	_____
Management	_____	_____	_____	_____
Payroll tax	_____	_____	_____	_____
Benefits	_____	_____	_____	_____
Advertising	_____	_____	_____	_____
Truck/auto expense	_____	_____	_____	_____
Contributions	_____	_____	_____	_____
Charge Costs	_____	_____	_____	_____
Dues & subscriptions	_____	_____	_____	_____
Freight	_____	_____	_____	_____
Insurance	_____	_____	_____	_____
Legal/acct.	_____	_____	_____	_____
Office supplies	_____	_____	_____	_____
Shop supplies	_____	_____	_____	_____
Travel	_____	_____	_____	_____
Telephone expense	_____	_____	_____	_____
Utilities	_____	_____	_____	_____
Repairs	_____	_____	_____	_____
Taxes/licenses	_____	_____	_____	_____
Rent/lease	_____	_____	_____	_____
Other expenses	_____	_____	_____	_____
Interest pmt.	_____	_____	_____	_____
Depreciation.	_____	_____	_____	_____
<b>Total G&amp;A Expense</b>	_____	_____	_____	_____
<b>Net income (pretax)</b>	_____	_____	_____	_____
Income tax:				
Federal	_____	_____	_____	_____
State	_____	_____	_____	_____
<b>Total taxes</b>	_____	_____	_____	_____
<b>NET INCOME</b>	_____	_____	_____	_____

## Exhibit VI-D: Pro Forma Balance Sheet

	<u>Year 1</u>		<u>Year 2</u>
	<b>ASSETS</b>		
<b>Current Assets:</b>			
Cash	_____		_____
Ending Inventory	_____		_____
Accounts Receivable	_____		_____
Other	_____		_____
Total current assets	\$ _____		\$ _____
<b>Fixed Assets:</b>			
Land	_____		_____
Building	_____		_____
Equipment	_____		_____
Machinery	_____		_____
Renovations	_____		_____
Furniture & fixtures	_____		_____
Other	_____		_____
Total fixed assets	\$ _____		\$ _____
Less accum. depreciation	\$ _____		\$ _____
Net fixed assets	\$ _____		\$ _____
<b>Other Assets:</b>			
Deposits	_____		_____
Other	_____		_____
Total other assets	\$ _____		\$ _____
<b>Total Assets</b>	<b>\$ _____</b>		<b>\$ _____</b>
	<b>LIABILITIES</b>		
<b>Current Liabilities:</b>			
Notes payable	_____		_____
Current portion long-term debt	_____		_____
Other	_____		_____
Total current liabilities	\$ _____		\$ _____
<b>Long-term Liabilities:</b>			
Loans payable	_____		_____
Less current portion	_____		_____
Total long-term debt	\$ _____		\$ _____
<b>Total Liabilities</b>	<b>\$ _____</b>		<b>\$ _____</b>
	<b>EQUITY</b>		
Owners' funds	_____		_____
Retained earnings	_____		_____
<b>Total Equity</b>	<b>\$ _____</b>		<b>\$ _____</b>
<b>Total Liabilities &amp; Equity</b>	<b>\$ _____</b>		<b>\$ _____</b>

## ***Exhibit VI-F: Break-Even Analysis***

(Projected using first year data)

SALES: \$ \_\_\_\_\_

COST OF GOODS SOLD: \$ \_\_\_\_\_

GROSS PROFIT: \$ \_\_\_\_\_

FIXED EXPENSES: \$ \_\_\_\_\_

NET PROFIT: \$ \_\_\_\_\_

STEP 1: Divide Gross Profit by Sales to show the percentage relationship.

$$\frac{\text{GROSS PROFIT}}{\text{SALES}} = \text{GROSS PROFIT AS A \% OF SALES}$$

STEP 2: Divide Fixed Expenses by Gross Profit as a % of Sales expressed as a decimal.

$$\frac{\text{FIXED EXPENSES}}{\text{GROSS PROFIT}} = \text{BREAK-EVEN IN DOLLARS}$$

## ***X. Developing Cash Flow, Balance Sheet and Income Statement Pro-Formas***

Developing financial pro-formas or projections is a vital aspect of your business plan. It is important that you take the time to thoroughly research your projections so that they will be as realistic as possible. Be liberal with your expenses and conservative with your revenues. It's much better if your financial surprises are pleasant ones.

Too often people try to determine their start-up costs before they consider their costs of operation after the business has opened. In order to finance properly, determine whether you will need additional cash at the outset to support periods of operating losses that often occur during the early months of operation. With that thought in mind, let's start our pro forma work with the cash flow statement.

A cash flow statement is nothing more than a presentation of the monthly cash receipts and cash disbursements that you expect to incur while operating your business. It is important to address this on a monthly basis because many businesses pay for their goods and expenses in one month but do not collect the money for selling those same goods for a month or longer. Numerous businesses fall in the cash flow trap. Also, many of your expenses are going to be fixed expenses - those expenses that stay the same regardless of your sales level. Fixed expenses might be rent, insurance, salaries or contract obligations.

While some businesses may generate "unearned" revenues such as rents, interest, or similar incomes, we will deal with the primary concern of most small businesses, sales.

### **1. SALES**

Sales revenue is that income your business receives by selling its goods and services to others. Your business may sell more than one type of goods and services, so you should keep your sales figures separated by product or service. Notice on the worksheet (Table 1) how sales are typically lower during the early months of operation. It will take time to develop a customer base for your business, so it will be necessary to borrow enough at the outset to carry the business through this building period. Your first step is to post projected monthly revenues to your cash flow statement.

### **2. CASH RECEIPTS**

Cash receipts reflect when you actually receive the cash for the goods that you sold. Some of your sales may be for cash, meaning that you receive those funds at the time of sale. However, some of your sales may be on credit, and you may be required to mail invoices for your sales. If this is true, then you have to "carry" the outstanding cash as accounts receivable. Some of this cash may be received in 30 days, some in 60 days, some longer; some of your accounts receivable may never be collected. All of these considerations must be brought into play when preparing the cash receipts section of your cash flow statement. It is the actual receipt of the cash that determines whether you have the cash on hand to pay your own bills.

### **3. DISBURSEMENTS**

It is now time to identify your monthly expenses. Be careful and realistic while considering these disbursements. The previous cash flow identifies some of the more common expense categories, but each business will experience its own peculiar expenses.



Of course, your cost of goods sold cannot be determined until you identify your expected revenues. Your research should have identified a "cost of goods sold" percentage for you. If that percentage was 50%, for example, then your cost of goods sold will be exactly one-half of your gross sales. If your cost was 25%, then your cost of goods sold will be one-fourth of your gross sales.

Be sure to remember that an increase in sales may bring about an increase in certain expenses. Sales increases may mean a need to hire additional labor, thus creating higher wages and benefits; it may also mean higher utility costs, higher material costs, and increases in other variable expenses.

#### 4. NET AND CUMULATIVE

Net cash flow reflects the difference between receipts and disbursements, positive or negative, for the current month. The cumulative cash flow, or current position, is determined by adding the present month's cash flow to that of the previous months.

*An example of a cash flow statement is shown on the next page. Note that the numbers in the narrative match the numbers on the worksheet. For example, "Disbursements," number 3 in the text is also number 3 on the worksheet (see Table 1).*

**Table 1: Projected Cash Flow Statement**

	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>6</u>
<b>Sales:</b>						
Sales No.1	\$10,000	\$11,000	\$11,500	\$12,000	\$12,500	\$13,000
#1      Sales No.2	\$ 5,000	\$ 5,500	\$ 5,775	\$ 6,000	\$ 6,200	\$ 6,500
Less returns						
<b>TOTAL SALES</b>	<u>\$15,000</u>	<u>\$16,500</u>	<u>\$17,275</u>	<u>\$18,000</u>	<u>\$18,700</u>	<u>\$19,500</u>
#2 <b>Total</b>						
<b>Acc'ts Receivable:</b>	\$27,250	\$16,125	\$17,081	\$17,819	\$18,525	\$19,300
#3 <b>Disbursements:</b>						
Cost of Sales	\$ 6,250	\$ 6,875	\$ 7,194	\$ 7,500	\$ 7,800	8,125
Labor	3,500	3,500	3,500	3,500	3,500	3,500
Management	1,800	1,800	1,800	1,800	1,800	1,800
Payroll Tax	636	636	636	636	636	636
Benefits	250	250	250	250	250	250
Advertising	500	500	500	500	500	500
Truck/auto expense						
Contributions						
Charge Card						
Dues & Subscriptions	25	25	25	25	25	25
Freight	126	126	126	126	126	126
Insurance	275	275	275	275	275	275
Legal/acct.	100	100	100	100	100	100
Office Supplies	35	35	35	35	35	35
Shop supplies	45	45	45	45	45	45
Travel						
Telephone	150	150	150	150	150	150
Utilities	450	450	450	450	450	450
Repairs						
Tax/license	55	0	0	0	0	0
Rent/lease						
Other expense	150	150	150	150	150	150
Principal pmt.	671	678	684	691	698	704
Interest pmt.	2,792	2,785	2,779	2,772	2,765	2,759
Add. Inventory						
Equipment						
Fixtures						
Other Assets - Dep.						
Other Assets						
Income taxes	0	0	0	0	0	0
<b>Total</b>	<u>\$ 17,810</u>	<u>\$ 18,380</u>	<u>\$ 18,699</u>	<u>\$ 19,005</u>	<u>\$ 19,305</u>	<u>\$ 19,630</u>
<b>NET CASH FLOW</b>	<b>\$ 9,440</b>	<b>(\$ 2,255)</b>	<b>(\$ 1,618)</b>	<b>(\$ 1,186)</b>	<b>(\$ 780)</b>	<b>(\$ 330)</b>
#4 <b>Plus: Working cap.</b>						
<b>at the begin. of the month</b>						
<b>CUMULATIVE</b>	<u><b>\$ 9,440</b></u>	<u><b>\$ 7,185</b></u>	<u><b>\$ 5,567</b></u>	<u><b>\$ 4,381</b></u>	<u><b>\$ 3,601</b></u>	<u><b>\$ 3,271</b></u>

	<u>7</u>	<u>8</u>	<u>9</u>	<u>10</u>	<u>11</u>	<u>12</u>
<b>Sales:</b>						
#1 Sales No.1	\$15,000	\$17,500	\$19,000	\$21,000	\$23,000	\$25,000
Sales No.2	\$ 7,500	\$ 8,500	\$ 9,500	\$10,500	\$11,500	\$12,500
Less returns						
<b>TOTAL SALES</b>	<u>\$22,500</u>	<u>\$26,000</u>	<u>\$28,500</u>	<u>\$31,500</u>	<u>\$34,500</u>	<u>\$37,500</u>
#2 <b>Total</b>						
<b>Acc'ts Receivable:</b>	\$21,750	\$25,125	\$27,875	\$30,750	\$33,750	\$36,750
#3 <b>Disbursements:</b>						
Cost of Sales	\$ 9,375	\$10,875	\$11,875	\$13,125	\$14,375	\$15,625
Labor	4,700	4,700	4,700	4,700	4,700	4,700
Management	1,800	1,800	1,800	1,800	1,800	1,800
Payroll tax	780	780	780	780	780	780
Benefits	250	250	250	250	250	250
Advertising	750	750	750	750	750	750
Truck/auto expense						
Contributions						
Charge Card						
Dues & Subscriptions	25	25	25	25	25	25
Freight	200	200	200	200	200	200
Insurance	275	275	275	275	275	275
Legal/acct.	100	100	100	100	100	100
Office Supplies	50	50	50	50	50	50
Shop supplies	65	65	65	65	65	65
Travel						
Telephone	200	200	200	200	200	200
Utilities	525	525	525	525	525	525
Repairs						
Tax/license	0	0	0	0	0	0
Rent/lease						
Other expense	200	200	200	200	200	200
Principal pmt.	711	718	725	732	739	746
Interest pmt.	2,752	2,745	2,738	2,731	2,724	2,717
Add. Inventory						
Equipment						
Fixtures						
Other Assets-dep.						
Other Assets						
Income taxes			750			1,000
<b>Total</b>	<u>\$22,758</u>	<u>\$24,258</u>	<u>\$26,008</u>	<u>\$26,508</u>	<u>\$27,758</u>	<u>\$30,008</u>
<b>NET CASH FLOW</b>	<b>(\$1,008)</b>	<b>\$ 867</b>	<b>\$ 1,867</b>	<b>\$ 4,242</b>	<b>\$ 5,992</b>	<b>\$ 6,742</b>
#4 <b>Plus: Working cap.</b>						
<b>at the begin. of the</b>						
<b>month</b>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
<b>CUMULATIVE</b>	<b>\$ 2,262</b>	<b>\$ 3,129</b>	<b>\$ 4,996</b>	<b>\$ 9,238</b>	<b>\$15,230</b>	<b>\$21,972</b>

# Sources and Uses of Funds

Having completed your cash flow worksheet, you now have some idea of what your sales and operating expenses might be and you can determine how much financing you will need.

## 5. USES OF FUNDS

Make a list of what you will need to purchase in order to begin operation, and determine the cost of each item. The Sources and Uses of Funds Statement shown in Table 2 gives some of the more common items that you must have before you start operation. Bids need to be secured for any construction, while pricing lists should be provided for equipment, machinery and inventory. Be sure to ask your local utility company if any deposits are required. Also, refer to your cash flow statement to see if you must prepare for period of cash shortage.

## 6. SOURCES OF FUNDS

After you have identified your financing needs, it's time to address where the funds must come from. Either the investor or investors must provide the necessary capital, or the business must make arrangements to borrow the funds. In most cases, you will use both sources of funds. (Our example (Table 2) shows that the entrepreneur has injected \$100,000 of his own funds. That is 25% of the entire project cost, which is approximately what a bank would require. The remaining 75% or \$300,000 was arranged through two separate loans: one long-term loan for the land and building, and a second, shorter-term loan for the equipment, machinery and fixtures.

## 7. CASH BALANCE

Obviously, the funds remaining after the initial purchases represent your working capital. As shown on the cash flow statement, this additional capital is necessary as a cushion to absorb the negative operating cash flow you have in your first seven months of operation (according to the examples in Table 1). Also, note that the \$16,000 cash balance on the Sources and Uses of Funds Statement is carried forward to your cash flow statement under the cash receipts (#2 section, Table 1).

**Table 2: Sources and Uses of Funds Statement**

<b>#6</b>	<b>Funds available</b>		
	Owner's funds .....	\$100,000	
	Loan #1 .....	250,000	
	Loan #2 .....	<u>50,000</u>	
	<b>Total</b>		\$400,000
<b>#5</b>	<b>Uses of funds</b>		
	Land .....	\$ 75,000	
	Building .....	250,000	
	Equipment .....	10,000	
	Machinery .....	25,000	
	Renovations .....		
	Inventory .....	10,000	
	Furniture and fixtures .....	10,000	
	Deposits .....	2,500	
	Other .....	<u>1,500</u>	
	<b>Total</b> .....		<u>\$384,000</u>
<b>#7</b>	<b>Cash Balance</b>		
	(Working capital)		<u>\$ 16,000</u>

## ***The Income Statement (The Profit and Loss Statement)***

With the cash flow worksheet completed, the income statement is easy to compile (see table 3).

### **8. SALES**

Total your monthly sales for each category as shown on your cash flow statement. This figure reflects your total annual gross sales. From this figure, deduct any refunds that you gave to customers for returned merchandise. This sum represents your total net sales.

### **9. COST OF GOODS SOLD**

How much did you have to pay to your suppliers for the products that you sold to your customers? This involves your inventory. Your Sources and Uses of Funds Statement should show how much inventory goods held for resale) you purchased to begin this operating period (\$10,000). If you are a new business, you had no beginning inventory because you did not exist before you started this period of operations. This figure is added to any purchases you made during the report period (\$118,994) to identify just how much you spent to have your goods available for sale. Suppose you did not sell everything you had in your inventory. At the end of this period you counted your inventor on hand and found that you still had \$10,000 of inventory on the date that your prepared the report. Your goods available for sale minus your ending inventory produces the total cost of goods sold (total material costs). In the example, that amounts to \$18,994 (\$128,994 minus \$10,000 of ending inventory).

### **10. GENERAL AND ADMINISTRATIVE EXPENSES**

These are the annual totals of the expenses as listed on the cash flow statement. Note that there are some changes. Payment of the principal portion of your notes is not considered an expense. It will be accounted for later on your balance sheet but does not appear on the income statement. Also, not the addition of an expense termed "depreciation." This is not considered on your cash flow statement because you don't write a check to depreciation. The purpose of depreciation is to account for the fact that your assets will begin to wear out as you use them. A certain piece of equipment may be expected to last for 10 years, for example. If that equipment cost you \$1,000 at purchase and will be worn out or worthless in 10 years, it is said "depreciate" \$100 per year. In our example the building, equipment, machinery, etc., is depreciated by \$11,400 per year. You don't actually write a check for the \$11,400, but your assets have devalued by that amount.

### **11. NET INCOME (Pre-Tax)**

Net sales minus material costs and operating costs gives us the net income of the business. However, this amount does not include the payment of taxes on the profit made.

### **12. TAXES**

If you have made a profit operating your business, you will be expected to pay both state and federal income taxes. This aspect of your business should be discussed thoroughly with your accountant.

### **13. NET INCOME (After-Tax)**

After taxes have been paid, the remaining profit belongs to your business in the form of retained earnings.

**Table 3: Projected Income Statement**

		<u>Year 1</u>	
		<u>Amount</u>	<u>% of Net</u>
<b>Sales:</b>			
#8	Sales No.1	\$ 190,500	66.73%
	Sales No.2	<u>94,975</u>	<u>33.27%</u>
	Gross Sales	\$ 285,475	
	Less Returns		
	<b>NET SALES:</b>	<u>\$ 285,475</u>	<u>100%</u>
#9	Cost of goods sold:		
	Beginning Inventory	\$ 0	
	Purchases	118,994	
	Additional Inventory	<u>10,000</u>	
	Goods Available	\$ 128,994	
	Less Ending Inventory <u>(10,000)</u>		
	<b>Total material cost</b>	\$ 118,994	41.68%
<b>G &amp; A Expenses:</b>			
	Labor	\$ 49,200	17.23%
#10	Management	21,600	7.57%
	Payroll tax	8,496	2.98%
	Benefits	3,000	1.05%
	Advertising	7,500	2.63%
	Truck/auto expense	0	0.00%
	Contributions	0	0.00%
	Charge Cards	0	0.00%
	Dues & subscriptions	300	0.11%
	Freight	1,956	.69%
	Insurance	3,300	1.16%
	Legal/acct.	1,200	.42%
	Office supplies	510	.18%
	Shop supplies	660	0.23%
	Travel	0	0.00%
	Telephone expense	2,100	0.74%
	Utilities	5,850	2.05%
	Repairs	0	0.00%
	Taxes/licenses	55	0.02%
	Rent/lease	0	0.00%
	Other expenses	2,100	0.74%
	Interest pmt.	33,059	11.58%
	Depreciation.	11,400	3.99%
	<b>Total G&amp;A Expense</b>	<u>\$152,286</u>	53.34%
#11	<b>Net income (pretax)</b>	\$ 14,196	4.97%
	Income tax:		
#12	Federal	\$ 1,500	
	State	250	
	<b>Total taxes</b>	<u>\$ 1,750</u>	0.61%
#13	<b>NET INCOME</b>	<u>\$ 12,446</u>	4.36%

## ***The Balance Sheet***

The balance sheet is a comparison of the assets, liabilities, and equity of your business. The one shown in Table 4 is a very basic example of a small business balance sheet.

### ***Assets***

#### **14. CURRENT ASSETS**

These are assets that are considered to be liquid or easily converted into cash. The cumulative cash of the business (#4) is listed along with the ending inventory (#9) and accounts receivable-as well as other similar assets-to form the current assets portion. The ending inventory is a listing of the goods held for sale at the end of your accounting period, and the accounts receivable is a listing of what is owed to you by your customers for previous purchases.

#### **15. FIXED ASSETS**

The second category of assets is fixed assets. This is a listing of the assets that are long-term in nature (brick-and mortar-type assets). It is these assets that depreciate in value over a longer period. Depreciation (\$11,400) for past period is therefore deducted from the sum of these assets and shown on the balance sheet as a accumulated depreciation.

#### **16. OTHER ASSETS**

This is a catchall section for other assets such as deposits held by utility companies.

#### **17. TOTAL ASSETS**

This is simply the sum of current, fixed and other assets (categories 14, 15, and 16).

### ***Liabilities***

Under the liabilities sections, you are dealing with what your business owes to others.

#### **18. CURRENT LIABILITIES**

Current liabilities are bills and accounts that you must pay within the next year. (Short-term notes or accounts payable are examples.) Also considered to be a current liability is that portion of any long-term note that must be paid during the upcoming year. This figure can be provided by your banker, accountant, or your amortization schedule of notes payable.

#### **19. LONG TERM LIABILITIES**

Long-term liabilities are by and large the long-term financial commitments your business has made to the bank or other debt holders. If additional debt is not incurred, the "notes payable" section will decrease each year by the amount of principal payments made during the period. In the example in Table 4, the original debt of \$300,000-as shown in the Sources and Uses of funds Section-is not reduced to a balance due of \$291,501. Therefore, \$8,499 in principal was paid during that first year of operation (\$300,000 minus \$291,501). Also, note that \$9,445 is deducted and shown as less current portion. That is because it is the portion of long-term principal that will be paid during the upcoming year, and it is therefore considered to be a current liability and is listed under that category.

#### **20. TOTAL LIABILITIES**

This is the sum of current and long-term liabilities.



## ***Equity***

### **21. EQUITY**

The equity section reflects your original investment (#6) as well as the accumulation of profits (#13) of the business (retained earnings).

### **22. TOTAL LIABILITIES AND EQUITY**

The sum of your liabilities and equity when added together should equal your assets. Do they balance? If not, you have an error in one of your sections.

**Table 4: Pro Forma Balance Sheet**

		<u>Year 1</u>
<b>ASSETS</b>		
<i>Current Assets:</i>		
	Cash	\$ 21,972
#14	Ending Inventory	10,000
	Accounts Receivable	9,375
	Other	<u>0</u>
	<b>Total current assets</b>	<b>\$ 41,347</b>
<i>Fixed Assets:</i>		
	Land	\$ 75,000
	Building	250,000
	Equipment	10,000
#15	Machinery	25,000
	Renovations	0
	Furniture & fixtures	10,000
	Other	<u>0</u>
	Total fixed assets	\$ 370,000
	Less accum. depreciation	<u>\$ 11,400</u>
	<b>Net fixed assets</b>	<b>\$ 358,600</b>
<i>Other Assets:</i>		
#16	Deposits	\$ 2,500
	Other	<u>1,500</u>
	Total other assets	<u>\$ 4,000</u>
#17	<b>Total Assets</b>	<b>\$ 403,947</b>
<b>LIABILITIES</b>		
<i>Current Liabilities:</i>		
	Notes payable	\$ 0
#18	Current portion long-term debt	\$ 9,445
	Other	<u>\$ 0</u>
	Total current liabilities	\$ 9,445
<i>Long-term Liabilities:</i>		
#19	Loans payable	\$ 291,501
	Less current portion	<u>(9,445)</u>
	Total long-term debt	<u>\$ 282,057</u>
#20	<b>Total Liabilities</b>	<b>\$ 291,501</b>
<b>EQUITY</b>		
#21	Owners' funds	\$ 100,000
	Retained earnings	<u>12,446</u>
	<b>Total Equity</b>	<b><u>\$ 112,446</u></b>
#22	<b>Total Liabilities &amp; Equity</b>	<b>\$ 403,947</b>

## Suggested Resources

1. Financial Studies of Small Business – Financial industry averages
2. The Risk Management Associates – Financial industry averages
3. *US Business Reporter* (<http://www.activemedia-guide.com/>) – Financial and Industry information
4. *Center for Business Research* (<http://cber.cba.ua.edu/>) – Alabama business information, Economic Abstract of Alabama, Alabama demographics, economic forecasts, economic research tools.
5. Household Spending (New Strategist = Publisher) – National and regional spending data.
6. *North American Industry Classification System (NAICS) codes* (<http://www.census.gov/epcd/www/naics.html>)
7. Government Information Website ([www.firstgov.gov](http://www.firstgov.gov))
8. Alabama Small Business Development Consortium ([www.asbdc.org](http://www.asbdc.org)) – Alabama Answers booklet, SBDC, etc.
9. ESRI Demographic Data
10. Hoover’s Online Service – Specific “for profit” business and industry information.
11. Greater Birmingham Regional Chamber of Commerce – Demographic, industry trend data.
12. Wall Street Journal Interactive Edition – Business, industry trend and financial information.
13. *Standard & Poor’s Guide to Industrial Surveys* – detailed industry history, current and future trending information as well as financial data.
14. Economic Development/Coordinators Office - Business, industry trend and financial information. Also location information, taxes, licenses and area planning information.
15. Small Business Administration ([www.sba.gov](http://www.sba.gov)) – financial, legislative and business training information.
16. *Entrepreneur Magazine* ([www.entrepreneur.com](http://www.entrepreneur.com)) – Small Business Encyclopedia, How to Guides, online business coaches, etc.
17. Entrepreneur Press ([www.entrepreneurpress.com](http://www.entrepreneurpress.com)) – Business library (books)
18. Alibris: Business, economics and new business enterprises - (<http://www.alibris.com/search/books/subject/Business%20Economics%20New%20Business%20Enterprises>)
19. Alabama Business Directory (<http://www.asbdc.org/books.htm>) – Comprehensive booklet containing great information on how to start and maintain a business in Alabama.
20. Encyclopedia of Associations – Worldwide guide to trade associations. Also lists publications and websites maintained by the trade associations.
21. Kiplinger Letters – Economic and political forecast information.
22. Kiplinger Forecasts ([www.kiplingerforecasts.com](http://www.kiplingerforecasts.com)) – Web based detailed economic and political forecast information.
23. Non-profit Resource Center of Alabama (<http://www.nrca.info/>) – Information on how to form and maintain a

non-profit business. Includes information on financing, training and management.

24. Central Alabama Women's Business Center (<http://www.cawbc.org/>) – Information on how to form and maintain a woman owned business. Organization provides training and information on financing and management of these types of businesses.