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Planning your business

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Planning is probably the most important aspect of operating a successful business. This is particularly true if you are just starting a small business. Unfortunately, planning is also one of the most overlooked management activities, especially in the initial stages of developing a small business. Small businesses don't have the luxury of a staff dedicated to the planning process; thus, planning falls on the shoulders of the busiest person in the business — you, the manager. Since starting the business places great demands on your time, planning can be easily forgotten unless given a high priority. The purposes of this publication are to convince you of the importance of developing a business plan and provide you with an outline and example of a financing proposal, which serves as a business plan.

A business plan

An adequately prepared business plan has several valuable uses. First, the process of preparing it forces you to think through the entire business operation, to consider the whole rather than the parts. Second, a well-prepared business plan is an excellent document to use as a guide or reference in the ongoing process of managing your business. Having thought through how to deal with various events allows you to anticipate change rather than be surprised by it. Finally, and perhaps most importantly, a business plan is needed to inform others about your business.

A financing proposal

A well-done financing proposal can serve as a business plan. As the manager of a small business, you will likely require financing at some time. Financing can take the form of loans (borrowed capital), investments (equity capital), or a combination of both. Most small business owners agree that obtaining financing is a difficult challenge, especially when starting a new business.

Your proposal for financing is a comprehensive document that explains your company's history, present condition, and plans for the future.

Since the proposal is a tool to sell your idea to others, it should be carefully prepared — accurate, persuasive, and professional-looking. Doublecheck all your numbers. Assume your audience knows nothing about your business or the product or service you will be selling. Explain things completely in terms everyone can understand. If problems exist, point them out and explain how you intend to solve them.

Be thorough, but be as brief as possible. Readers should not have to wade through nonessential material to get to the important information. Supporting documentation is a good idea if it clearly helps the reader understand the plan, but, generally, it should be included as an appendix and referred to in the text.

The proposal must be neatly typewritten on 8 1/2 x 11-inch paper. Supporting documentation may be odd-sized, but the entire proposal should be bound in a cover.

The proposal demonstrates your skills with regard to the fiscal and managerial abilities needed to operate a successful business. Also, in preparing the proposal you will likely see your company from a different perspective, and you may uncover weaknesses in your plan. Identification of problems at an early stage allows you to plan for corrective action in the future. Although time consuming, the creation of a financing proposal is a good investment in the future of your business.

The following outline of a financing proposal uses a diversified farm as an example. The outline and example apply to an existing business that plans to start a new enterprise. A new business would present the same information with the exception of the historic business data.

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322
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Outline for a financing proposal

I. Title page

The title page should be the front cover of the document (Example 1). You may want to use special spacing or larger type to give the title page a formal appearance.

Example 1

Financing Proposal for New Enterprise Farm

Example 2

Financing Proposal for New Enterprise Farm

Table of Contents

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II. Table of contents

The table of contents should follow the title page (Example 2).

III. Summary

Try to summarize in two pages or less (Example 3). A brief summary lets the financing officer quickly determine if your proposal warrants further consideration. Include the following: date, name, and location of the business; type of ownership (sole proprietorship, partnership, or corporation); amount of financing required; length of time for repayment and frequency of payments; source of repayment (profits, sale of certain assets, etc.); type of collateral offered to secure the loan (real estate, equipment, assignment of equity, etc.); names of persons who will give a personal guarantee; and how the funds will be used in the business.

Example 3

Financing Proposal for New Enterprise Farm

February 1, 1992
Summary

New Enterprise Farm is a sole proprietorship of Jonathan and Emily Doe located at Route 5, Box 27, Ruraltown, Idaho. The firm requests financing in the amount of a \$50,000 line of credit repayable in annual installments over 10 years beginning 5 years after loan proceeds become available. Source of repayment will be profits from the addition of a 2-acre blueberry enterprise. Collateral will be a first lien on \$17,500 worth of farm equipment and a second lien on the 250-acre farm (market value of \$235,000 with a first mortgage of \$83,000).

New Enterprise Farm has been a successful business for 16 years, selling cattle, hay, and Christmas trees. The addition of 2 acres of blueberries will generate additional income and diversify the firm's income sources.

The requested funds will be used for the purchase of additional specialized farm equipment, installation of a 2-acre drip irrigation system, establishing the blueberry stand, and maintaining the stand for 4 years until production is sufficient to cover operating costs.

IV. Business description

Describe your company in detail (Example 4). Indicate how long it has been under your ownership or management. Discuss the products or services sold. If the business is unique in any way, be sure the reader can understand the nature of your product or service and its use or application — a unique operation may require photographs, drawings, brochures, or other materials as supporting evidence. Give a description of the facilities associated with the business, any special features, and lease terms if applicable.

V. Management

Provide names and titles of the individuals responsible for the day-to-day operation of the business, including their areas of responsibility. Include a resumé for each individual, giving the education, training, and experience that qualify them for their specific assignment (Example 5). Any employees (or other family members) involved in the business that have expertise valuable to the company should be mentioned. Most lenders and investors consider strong management to be a critical factor in the success of any business. Proposals that are

otherwise sound can be rejected solely on the basis of a perception of weak or inadequate management.

VI. Your market

Provide proof that a market exists for the product or service to be offered (something more concrete than "all my friends think it's a good idea"). Obtaining good

market information can be a challenge. Some sources are local libraries, nearby wholesalers and suppliers, professional or trade associations, government agencies that deal with commerce, and economic development or taxation entities. Information must be as specific and accurate as possible (Example 6). You should name sources.

Example 4

Description of Business

New Enterprise Farm was established by the present owners in 1975 with the purchase of a small cattle and hay operation with 250 acres of deeded land. The cattle and hay operation involves late fall and early spring pasturing and overwintering about 100 head of stocker cattle using hay produced on 100 acres of hay ground. Additional pasture is rented on an availability basis in the fall and spring. Surplus hay is sold in late winter and early spring.

The farm is located along a state highway about 40 miles northeast of Spokane, Washington, and is 7 miles off Idaho Highway 95. In 1980, New Enterprise Farm

diversified by establishing a successful 10-acre cut-your-own Christmas tree operation. Currently, cattle and hay account for about 60 percent of total cash receipts, and Christmas trees account for the other 40 percent. The owners have been successful in their efforts to diversify into Christmas trees and plan to further diversify by establishing a blueberry operation.

The 2-acre blueberry operation will require the purchase of additional equipment, installation of a drip irrigation system, and establishing/maintaining the stand over a 5-year period. Full production will begin in year 5, and the stand is projected to last 20 years.

Example 5

Management

A short vita of Jonathan Doe and Emily Doe follow. Complete resumés are included in the appendix. Both individuals play a part in managing the firm and each is capable of performing the overall management function. Currently, Emily is responsible for recordkeeping,

livestock purchasing, and marketing the livestock. Jonathan handles the day-to-day activities of the entire operation and is responsible for the Christmas tree enterprise. Both individuals are involved in long-range planning.

Jonathan Doe

Emily Doe

WORK EXPERIENCE

1975-present New Enterprise Farm, owner/manager
 1975-present Smith Christmas Tree Farm, seasonal worker
 1970-75 Blue River Ranches, ranch gardener/groundskeeper

New Enterprise Farm, owner/manager
 Lakeside Enterprises, part-time bookkeeper
 Blue River Ranches, ranch herd manager

EDUCATION

1986-87 Alternative enterprise short course, University of Idaho Cooperative Extension
 1970 Associate degree, Horticulture, Treasure Valley Community College, Ontario, Oregon

B.S. degree, Animal Science, University of Idaho, Moscow, Idaho

OTHER EXPERIENCE

Raised on a fruit ranch in southwestern Idaho and worked summers in area orchards

Raised on a cattle ranch in eastern Washington and worked summers on family ranch

Topics to be considered (not all will apply in every case) include:

- Market location and size in terms of geography, population, and dollar and/or unit sales for your type of goods. Include detailed data on population characteristics if your product or service is targeted to a specific group of users.
- Market trends (historic and projected) and an indication of your firm's sales (or expected sales) compared to these figures (market share).
- Names, locations, and strength of competition. Compare the strengths and weaknesses of the competition to your proposed business.
- Patents, copyrights, or other proprietary rights.
- A discussion of your strategy for competing in the market (for example, pricing, product quality, service, location, transportation, etc.).
- Types of licenses required to market your product or other government regulations that may impact marketing activities.
- Results of any test marketing.
- Plans for promotional or advertising activities.
- Any major changes in the market expected over the next several years.

Example 6

Market for Blueberries

Blueberries will be sold into three markets. At full production, the 2-acre stand will produce about 12,000 pounds of blueberries over a 6-week harvest season. The highest quality fruit (about 30 percent of the crop) will be hand picked and sold to upscale restaurants in the Spokane and Coeur d'Alene areas. Local labor currently used in the Christmas tree operation is available for picking and sorting of berries for the upscale market.

Initial contact with eight restaurants (see appendix) allows estimation of a market of 80 to 100 pounds per day in the range of \$2.00 to \$2.50 per pound for fresh, local blueberries of high quality. Currently, these restaurants are obtaining fresh blueberries from the coast of Washington state through produce wholesalers. None of the restaurants currently purchase fresh blueberries from the local market. However, all of them indicated a preference for a fresh, high-quality local product and a willingness to pay a premium of 50 to 75 cents for such a product.

A pick-your-own market will be used for the majority of sales (about 60 percent of the crop). Survey data from existing Christmas tree customers (complete results are included in the appendix) indicate a solid market for 5,000 pounds of U-pick blueberries in the \$1.00 to \$1.50 price range. Advertising beyond the existing Christmas tree customer base is expected to generate additional sales of at least 2,000 to 3,000 pounds in the same price range.

Competition for the U-pick blueberry market is limited within this region. The only substantial pick-your-own operation (Blueberry Knob) is 12 miles north of New Enterprise Farm. Blueberry Knob has been in operation for 9 years, focuses exclusively on pick-your-own blueberries, and has almost 5 acres in production. The firm appears to rely heavily on repeat customers. Fliers mailed to existing customers providing dates when blueberries will be ripe is the primary method of advertising. Blueberry Knob is located on an unpaved county road and is 12 miles further from major population centers compared to New Enterprise Farm.

Small quantities of blueberries are also produced in the Greenbluff area north of Spokane. This area focuses on pick-your-own operations for a variety of fruits and vegetables. Many producers take part in an organized cooperative effort to promote this area for U-pick produce. However, blueberries represent an insignificant component of the area's total production of produce.

Lower quality berries (sort-outs from the high-quality market) and berries left from the pick-your-own market will be sold to a local firm (Idaho Foods, Inc.) selling manufactured "Idaho" food products. This market is expected to handle the 1,000 to 2,000 pounds of berries not sold in the two primary fresh markets. Price will need to be in the range of 70 to 75 cents per pound to compete with other berries.

The market for locally produced fresh produce has grown over the past several years along with increases in the area's population. National trends point toward increased consumption of fruits and vegetables, more diversity in the diet, and greater consumption of fresh foods. Fresh blueberries are an ideal match to satisfy these changing demands. The recent addition of a commercial kitchen at the Bonner Business Incubator in Sandpoint, Idaho, suggests additional processing demand may develop over time.

New Enterprise Farm has established itself as a quality producer in the U-pick Christmas tree market. The firm has traditionally focused on quality in regard to both customer service and product. Location, convenient access, and availability of surface water will allow the firm to maintain a competitive price structure for blueberries.

Regulation for firms producing and selling their own fresh produce is minimal. Contacts with the county health offices for Kootenai and Spokane counties indicate they do not regulate farm products sold in fresh form. The Idaho and Washington Departments of Agriculture have also been contacted. Both agencies indicate there are no permits required or quarantine restrictions on blueberries if grown and sold by the same firm.

VII. Use of Funds

An explanation of the use of requested funds make up this section. Expenditures for the purchase of land, equipment, or construction or remodeling should be described to provide a good understanding of the project (Example 7). Include legal descriptions for land purchases, sales brochures for equipment, and plans and estimates (or bids) for construction. Provide a brief explanation of the needs that will be met and the expected benefits from use of the funds.

Example 7

Use of Funds

The requested \$50,000 will be used to meet the following needs:

Year 1

- \$17,500 — Equipment: 24 hp tractor, rotary tiller, mower, and fertilizer spreader (see appendix for sales brochures with a complete description)
- \$10,500 — Install drip irrigation system on 2 acres
- \$ 7,000 — Land preparation, install deer fence, plant 2 acres

Years 2 through 4

- \$ 5,000 — Annual maintenance costs before full production (total cost of \$15,000)

Example 8

Description of Loan Collateral

1. First lien on \$17,500 of equipment to be purchased. Equipment is described in the "Use of Funds" section, and precise information is provided in the sales brochures in the appendix.
2. Second lien on 250-acre farm located at Route 5, Box 27, Ruraltown, Idaho. A complete legal description and title company sketch are provided in the appendix. The property is appraised for tax purposes at \$175,000. A market appraisal completed this year (see appendix) established market value at \$235,000. The first lien on the property in the amount of \$83,000 is held by Federated Security Bank of Spokane, Washington.

VIII. Collateral

The summary includes mention of your collateral, but a more detailed list is generally necessary (Example 8). Identify equipment by make, model, year, and serial number (if applicable). Provide locations of real estate with size and physical improvements. A copy of the legal property description with a title company sketch or plat map may be included in the appendix. Show cost, book value, and estimated market value for all presently owned collateral. Refer the reader to the "Use of Funds" section or the appendix for the description of property or equipment to be purchased with the loan.

IX. Financial exhibits

The following financial reports should be included with your proposal (Examples 9-12):

- Year-end balance sheets (statement of financial condition) and profit and loss reports (statement of income and expenses) for the past 3 years, or for whatever time the business has existed, if less than 3 years. If you are establishing a new business venture, personal financial statements and tax returns will likely be needed.
- A profit and loss projection and cash flow projection representing the period of time over which the funds will be repaid. These projections will illustrate the effect of the requested funding on the company's earnings, and its ability to meet its debts without additional borrowing. The projections should be consistent with the market data in section VI.
- Assumptions explaining how you arrived at the numbers used in the projections. For example, an existing business may use historical sales data plus a percentage increase and explain the basis for the increase. These explanations should be done not only for sales and operating costs, but for each item in the projection that is controllable. The purpose of these explanations is to provide the reader with sufficient information to judge the reality of the projections.
- Pro forma balance sheet showing what the company's financial position will be if the funding is approved.
- Personal financial statements of individuals who will guarantee the loan (if applicable). Keep in mind that business and personal income tax returns may be requested for up to the 3 preceding years.

Example 9

Income Statement New Enterprise Farm

	Year ending 31 Dec 89 (\$)	Year ending 31 Dec 90 (\$)	Year ending 31 Dec 91 (\$)
Commodity sales			
Cattle	68,250	71,175	65,720
Hay	5,750	2,380	7,650
Christmas trees	<u>31,500</u>	<u>41,400</u>	<u>48,275</u>
Total sales	105,500	114,955	121,645
Operating costs			
Livestock purchases	52,250	53,180	48,150
Labor expense	10,450	11,075	15,080
Equipment operating costs	10,750	9,350	11,775
Pasture rental	3,600	2,780	5,800
Interest expense	2,200	3,200	2,120
Miscellaneous expenses	<u>1,200</u>	<u>1,375</u>	<u>1,980</u>
Total operating costs	80,450	80,960	84,905
Fixed costs			
Mortgage	7,500	7,500	7,500
Depreciation	1,500	1,500	1,500
Christmas tree establishment cost	<u>8,500</u>	<u>8,500</u>	<u>8,500</u>
Total fixed costs	17,500	17,500	17,500
Total costs	97,950	98,460	102,405
Net income	7,550	16,495	19,240
Owners' withdrawal ¹	6,000	10,000	14,000

¹Withdrawals from the business are supplemented by off-farm earnings to meet family living expenses. See personal tax returns in appendix.

Example 10

Balance Sheet New Enterprise Farm

	31 Dec 89 (\$)	31 Dec 90 (\$)	31 Dec 91 (\$)
Assets			
Current assets			
Cash	2,150	3,275	1,126
Accounts receivable	750	820	1,120
Livestock inventory	60,000	65,000	58,000
Hay inventory	10,500	12,250	14,250
Other current assets	<u>1,175</u>	<u>1,250</u>	<u>1,650</u>
Total current assets	74,575	82,595	76,146
Noncurrent assets			
Land and improvements	185,000	185,000	185,000
Equipment (net of depreciation)	<u>27,500</u>	<u>28,500</u>	<u>31,700</u>
Total noncurrent assets	212,500	213,500	216,700
Total assets	287,075	296,095	292,846
Liabilities			
Current liabilities			
Accounts payable	5,621	7,650	8,250
Operating notes payable	71,500	67,750	72,650
Taxes payable	<u>8,750</u>	<u>12,675</u>	<u>13,765</u>
Total current liabilities	85,871	88,075	94,665
Noncurrent liabilities			
Land mortgage	94,725	88,862	83,000
Total liabilities	180,596	176,937	177,665
Net worth	106,479	119,158	115,181

Example 11

Projected Income Statement New Enterprise Farm

(Blueberry enterprise at full production)

	Year ending 31 Dec 97 (\$)
Commodity sales¹	
Cattle	70,000
Hay	4,500
Christmas trees	50,000
Blueberries	<u>21,000</u>
Total sales	145,500
Operating costs²	
Livestock purchases	50,000
Labor expense	12,000
Equipment operating costs	12,000
Pasture rental	4,000
Interest expense	3,000
Miscellaneous expenses	1,200
Blueberry operating costs ³	<u>3,800</u>
Total operating costs	86,000
Fixed costs⁴	
Mortgage	7,500
Depreciation	2,200
Christmas tree establishment cost	8,500
Blueberry establishment cost ⁵	<u>9,350</u>
Total fixed costs	27,550
Total costs	113,550
Net income	31,950

¹Cattle and hay sales are based on historic 5-year average. Christmas tree sales reflect an expected 15 percent increase in price coupled with a 13 percent decline in production. Blueberry revenues are based on the marketing program presented on page 4.

²Operating costs are maintained at average levels except for interest costs, which are increased by \$800 to reflect the needed higher operating credit line and higher interest rates.

³Blueberry operating costs are based upon the University of Idaho College of Agriculture blueberry budget (see appendix) with harvesting costs adjusted to reflect a pick-your-own-operation.

⁴Fixed costs reflect a higher depreciation expense due to the addition of new equipment. Other fixed costs are unchanged.

⁵The blueberry establishment payment reflects a 10-year amortization schedule beginning in 1997 for the \$50,000 credit line plus interest from 1992 until 1997 (\$62,734 amortized over 10 years at 8 percent).

Example 12

Pro Forma Balance Sheet New Enterprise Farm

31 Dec 92
(\$)

Assets	
Current assets¹	
Cash	2,250
Remaining credit line	15,000
Accounts receivable	1,150
Livestock inventory	60,000
Hay inventory	16,000
Other current assets	<u>1,800</u>
Total current assets	96,200
Noncurrent assets²	
Land and improvements	190,000
Equipment (net of depreciation)	<u>46,300</u>
Total noncurrent assets	236,300
Total assets	332,500
Liabilities	
Current liabilities	
Accounts payable	10,000
Operating notes payable	75,000
Taxes payable	<u>14,000</u>
Total current liabilities	99,000
Noncurrent liabilities	
Land mortgage	77,200
Blueberry credit line	<u>50,000</u>
Total noncurrent liabilities	127,200
Total liabilities	226,200
Net worth	106,300

¹Current assets are based on a 5-year average for commodity inventories. Cash and accounts receivable are increased by 10 percent above average to account for additional volume of Christmas tree sales. The unused portion of the credit line is recognized as an asset since the entire credit line (\$50,000) is recognized as a liability.

²Land and improvements are increased by \$5,000 to reflect the market value of the installed drip irrigation system. Equipment value represents an increase of \$17,500 for the additional purchases less depreciation.

X. Appendix

The appendix contains supporting documentation that will assist the reader in fully comprehending your proposal (Example 13). The text of the proposal should contain selected information to maintain brevity — more complete information about the owners, market analyses, collateral descriptions, etc., should be available in the appendix. The first page of the appendix should be a table of contents of listing the information included.

Example 13

Appendix

1. Resumés for Jonathan and Emily Doe
2. Fresh blueberry market survey of restaurants
3. Fresh blueberry market survey of Christmas tree customers
4. University of Idaho cost of production budget for blueberries in northern Idaho
5. Equipment description brochures
6. Legal description and survey sketch of deeded property
7. Market appraisal of deeded property
8. Current mortgage on deeded property
9. Personal income tax returns for Jonathan and Emily Doe (1989-91)

For further reading

Miller, Neal. *Your Small Business Financing Proposal*, 3rd ed. Small Business Development Center, Washington State University, 245 Todd Hall, Pullman, Washington 99164-4727.

Sargent, Dennis J., and Maynard N. Chambers. *Your Idaho Business Plan*. Idaho Small Business Development Center, Boise State University, 1910 University Drive, Boise, Idaho 83725.

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