

THE ERNST & YOUNG

Business Plan Guide

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Sold**

THIRD EDITION

Featuring...

- Advice on how to write and develop business plans
- A realistic sample plan
- All new sections on funding and financing methods with provisions for restructuring and bankruptcy
- Tips for tailoring plans to the decision makers

Brian R. Ford Jay M. Bornstein Patrick T. Pruitt

Preface

This book has a heritage back to the early 1980s, the time of Reaganomics, entrepreneurship, and a renewed sense of spirit in our country. It was prepared for the thousands of people starting businesses. At the time, there were few resources available to entrepreneurs to help them develop their first business plan. This book was written to fill that void. It has been published in many languages around the world and has been well received.

In order to broaden the appeal, this new edition has been prepared for entrepreneurs who are in the planning stages of starting, expanding, or acquiring a business. We provide a step-by-step process for preparing a business plan. The instruction goes beyond simply discussing what is required in such a proposal. It explains why certain information is required, how it may be best presented, and the sensitivities of both the preparer and reviewer.

Since the first edition was published in 1988, the authors have heard from many entrepreneurs about the importance of this straightforward approach to the business plan, which not only helps entrepreneurs tell their stories but creates the discipline to be sure each story is complete and has all the elements necessary to enhance its success. While not the original intent, we have also heard from many that it helps mature business leaders present a plan for capital resources within larger companies.

We believe the discipline of a start-up business plan is not radically different from the planning associated with a new business venture within a large organization. In response, from the advice of investors and from entrepreneurs who have used this book, one of our efforts on this edition is to

provide more of the investor's perspective. Second, readers suggested that while we helped entrepreneurs with the business plan and helped them anticipate the needs of the potential investor, we could go somewhat further to better explain the investor's outlook. The "whys" of what should be in a business plan are now emphasized more.

Many entrepreneurs underestimate the importance of writing a business plan. They underestimate how much having a good business plan can help a business raise money to start or expand, plan for the future, and keep tabs on how it is currently progressing. In this book, we not only stress these important aspects of business plans, but help the entrepreneur think through and prepare a business plan that serves all three purposes.

Launching a business venture is a serious undertaking. While statistics on the failure rate of new businesses vary, all suggest a high incidence, particularly in the first few years. Acquisitions of existing businesses or product lines and expansions of present operations enjoy a significantly higher success rate, due to the lesser degree of uncertainty. However, even in these circumstances, issues are complex and stakes are high.

In light of this, entrepreneurs must act in whatever manner will improve these odds. In almost every instance, this suggests the meticulous creation and adherence to a business plan. The exercise of writing a business plan forces the entrepreneur to examine each element of his or her prospective venture closely. It is expected that many cracks and flaws will be identified and addressed through this process.

Where such problems cannot be addressed and where their ramifications are significant, the fact that they have been identified affords the entrepreneur an opportunity to

abandon the venture before resources have been committed.

In the first three chapters of this book, some of the basics of business plans are laid out. [Chapter 1](#) asks: What is a business plan? A business plan has more purposes than the one most people think of first—that of raising money.

Many entrepreneurs misunderstand who reads a business plan and what those readers are looking for. In [Chapter 2](#), we discuss both lenders and investors, and how they evaluate a business plan.

[Chapter 3](#) deals with the legal form a business may take. What form a business takes is an important determinant of the amount of money that can be raised for the business and from whom, the form of the infusion, the impact the federal tax code will have on the business, and the potential financial rewards for investors.

In [Chapter 4](#) we look at a twenty-first-century creation: the trend toward business sellers hiring an analyst to do one single “reverse due diligence” analysis in order that all potential buyers have the same information and to avoid a situation where each potential buyer’s expert is upsetting the running of the selling company by continually seeking the same information from managers and executives.

The vast majority of this book, beginning with [Chapter 5](#), consists of a piece-by-piece dissection of a model business plan. In each of these chapters, we examine a portion of the business plan. We suggest how entrepreneurs should structure and present parts of the plan. We raise questions and issues to which an entrepreneur must be sensitive when preparing the plan. Finally, we raise questions that might be asked by an individual who reviews the plan.

In each of the chapters that deal with a specific part of the business plan, we provide a general narrative dealing with

how to think through and prepare this portion of the plan. A portion of a model business plan is then presented. The business plan we use is for Good Foods, Inc. (GFI), an all-natural baby and children's food company. The plan is hypothetical and has been prepared by the authors as an example for illustrative purposes. After each section of the GFI business plan is presented, we comment on it, pointing out its strong and weak points. The likely reactions of reviewers are also presented. The three sections of each chapter are presented in three different styles for ease of reading. We believe this book will be valuable in the development of a professional and effective business plan.

Brian R. Ford
Jay M. Bornstein
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Philadelphia, Pennsylvania
April 2007

A DEDICATION TO ENTREPRENEURSHIP AND THE ENTREPRENEURS OF AMERICA

It's people like you who help make our nation great. Our country continues to look toward you, our country's entrepreneurs, for inspiration.

In good times and bad, you climb your own personal Mount Everest, and settle for nothing less than reaching the top.

Why? Because you have what it takes to succeed! You keep your eyes on the summit and you won't quit! If you stumble, you get up, dust yourself off and keep going!

To paraphrase the words of Robert Kennedy:

Some people look at things the way they are and ask why?

You're the people who dream of things that never were and ask why not?

America is called the land of opportunity. Looking at our entrepreneurs, we know that's true. We've read your inspiring stories. They're truly amazing.

Your integrity and commitment to quality—two attributes that continue to be of the utmost importance—set you apart:

Each of you has taken advantage of an opportunity, or more likely, several opportunities over the course of your careers. When a friend said to the great entrepreneur Steve Wynn, "An opportunity like that does not come along every day," Steve responded, "If you're good, you only need one." Steve has seized many opportunities!

And in doing so, you've created opportunities for families, friends, employees, and your communities.

When you think about it, just about everything starts with an entrepreneur's vision and execution.

Even today's multinational giants were once entrepreneurial in nature—FedEx, Genentech, Intel, Adobe Systems, to name just a few. They started out just like you and look at them now.

In 1899 a government official in the United States suggested something novel: that the U.S. Patent Office be closed forever. He said, "Everything that CAN be created has been created." Anyway, he never thought of people like you.

The number of innovations in the last 100 plus years is truly amazing. Airplanes, automobiles, wonder drugs, television, and computers. The list goes on and on and on. That's because entrepreneurs are not constrained by preconceived notions.

They imagine the unimaginable!

They embrace change!

Or they create it themselves!

Entrepreneurism is the American way!

ABOUT THE AUTHORS

Brian R. Ford, a partner in the Philadelphia office of Ernst & Young, has many years of experience in providing services to entrepreneurial businesses. He has been instrumental in the early development of our practice, a full-service organization specifically designed to provide services to growing businesses and serving the strategic growth markets in Philadelphia. He has worked with entrepreneurs from their “idea” stage to beyond their initial public offering. His career has been varied from mutual funds, to manufacturing, retail, and distribution. He has served Fortune 25 clients and has extensive expertise in the supply chain. For many years he has served as the firm’s leader for services to the casino gaming industry and is a leading expert in this industry. Brian is one of the original authors of *The Ernst & Young Business Plan Guide*.

Jay Bornstein, a tax partner in the Philadelphia office of Ernst & Young, has served as a tax adviser to entrepreneurial businesses and their owners for over 20 years. His clients include start-up businesses that eventually grew to become publicly traded companies to management buyouts of business units of some of the country’s largest companies. Jay joined the author team for *The Ernst & Young Business Plan Guide* for the second edition, published in 1993.

Patrick T. Pruitt, a partner in the Philadelphia office of Ernst & Young, is the newest member of *The Ernst & Young Business Plan Guide* author team. He has spent his entire professional career working in Ernst & Young’s Strategic Growth Markets practice, where he has assisted companies in all stages of the business cycle. He has extensive experience working with companies on financing

alternatives, including obtaining early-round angel financing, private-equity financing, and entry into the public-capital markets.

ABOUT ERNST & YOUNG'S STRATEGIC GROWTH MARKETS PRACTICE

Ernst & Young's Strategic Growth Markets practice is the leader in serving the Russell 3000, which are high-growth private companies, companies with significant investments from venture capital or private-equity firms and companies planning to go public. We are committed to serving entrepreneurial companies throughout their life cycle—from promising start-ups through their growth into successful market leaders.

Quality in Everything We Do. Ernst & Young's integrity and professional competence are the cornerstones of our global organization. We work hard to earn and maintain our clients' trust and confidence. To ensure that we provide quality professional services in an independent, objective, and ethical manner, we have implemented a number of global professional development initiatives and quality and compliance safeguards.

Services Offered. Ernst & Young provides a range of services, including accounting and auditing, tax reporting and operations, tax advisory, business risk services, technology and security risk services, transaction advisory, and human capital services. Our foreign country practices also provide legal services in those parts of the world where permitted.

Culture. Ernst & Young would not be such a successful organization without great people and strong teamwork. We provide our people with solid career growth opportunities and a people-oriented workplace environment. Our philosophy, quite simply, is that when our

people achieve their best, so do our clients, and our business prospers.

THE ERNST & YOUNG ENTREPRENEUR OF THE YEAR PROGRAM

En-tre-pre-neur: From the thirteenth century French verb *entreprendre*, meaning “to do something” or “to undertake.”

Like so many entrepreneurial ventures, the Entrepreneur of the Year (EOY) program began as a way to recognize the best in the business world. The idea quickly grew from a fledgling success to an established program honoring entrepreneurial excellence. The year 2006 is the twentieth anniversary of the Entrepreneur of the Year awards. Today, it is a proud tradition that has expanded to more than 100 cities in 39 countries, with annual awards presented to the world’s most successful and innovative entrepreneurs. It is the world’s most prestigious business award.

Being a recipient of this prestigious award means that you’re at the top of your game, joining award winners that already include such pioneers and innovators as Michael Dell of Dell Computer Corporation; Scott Kriens of Juniper Networks; Pierre Omidyar of eBay, Inc.; John Mackey of Whole Foods Market; Wayne Huizenga of Huizenga Holdings, Inc.; Maxine Clark of Build-a-Bear Workshop; Catherine L. Hughes and Alfred Liggins of Radio One, Inc.; Jim McCann of 1-800-Flowers.com; and other leaders and visionaries who create and build world-class businesses. These are the men and women whose achievements are a testament to their vision, tenacity, and leadership—whose accomplishments raise the bar and often change the face of an industry.

Who Is Eligible?

For complete information regarding the Ernst & Young Entrepreneur of the Year program, including eligibility, program locations, and a process description, please go to the EOY Web site at ey.com/us/eoy.

PART I



The Purpose of a Business Plan

In this section, we discuss the basic purposes of a business plan, how the business plan is used as a tool for securing financing, and how to think through the issue of the proper legal form for a newly created or defined business.

[Chapter 1](#) covers the business plan in general. Many people think that the business plan is the unique province of start-up companies and entrepreneurs. In reality, a business plan is an integral tool for any business (or any not-for-profit entity as well) as a way to map out a desired short- and medium-term future.

Large companies often demand comprehensive annual business plans from each division or operating entity in order to allocate corporate resources. A company looking to buy or merge with another entity needs a business plan that shows the implications of such a combination and how the unified business will operate going forward. On the flip side, a company selling off a unit needs a business plan of how it will operate without the sold-off portion.

Companies should require a business plan for any new operating group, division, or subsidiary being formed, and some businesses require a business plan for every new product or project. Indeed, our publisher required of our editor a business plan for this book that detailed content, marketing, distribution, costs, and projected revenues.

[Chapter 2](#) deals with the business plan as a specific tool for acquiring financing for a new or growing privately held business. Just as businesses use business plans to allocate

corporate resources within the company, independent investors such as venture capitalists, private equity firms, and “angel” investors, as well as lenders such as banks or finance companies, use business plans to allocate resources to freestanding businesses. If a company is offering stock to the public, or to more than a few independent investors, the Securities and Exchange Commission (SEC) gets involved and spells out what must be included in a special form of business plan, known as a prospectus, that each potential investor must receive.

Since the last update of this book in 1993, the universe of potential investors in privately held businesses has exploded, as private equity groups, hedge funds, and even endowments and pensions have increased their exposure to equity investments in businesses not publicly traded. While venture capitalists and angels have often been seen as “gut feel” investors, because of their heavier fiduciary burden, these new players are often more demanding of detailed and specific business planning before they will invest.

[Chapter 3](#) takes on the issue of the many legal forms a business may take on its founding. The choice of legal form is driven by four general considerations: liability, control, ease of admitting new investors, and taxes. In the 20 years since the first edition of this book appeared, there have been almost countless legislative changes to the United States tax code, as well as numerous legal interpretations of federal, state, and even foreign tax laws as they apply to U.S. businesses.

Perhaps the largest change in legal entity form over the last 20 years is the advent of the limited liability company (LLC). The LLC is often described as a “hybrid” of a partnership and a corporation, and has become the favorite form of legal entity for small businesses, and even for some larger businesses. LLC laws are governed by each state.

Wyoming was the first state to enact an LLC statute, in 1977, which sought to afford small-business owners the legal protection of corporate owners without all of the paperwork. According to the *Wall Street Journal*, over 300,000 LLCs were formed in 2005 and their total number doubled between 2001 and 2004. The LLC seems to have supplanted the S corporation as the preferred legal form for entrepreneurs.

Finally, [Chapter 4](#) discusses a concept known as “reverse due diligence.” Business plans are written by companies prior to acquiring another company, in an effort to understand how that new company will fit in with the acquiring company’s other corporate pieces. In a situation where a company puts itself up for sale, it may have a half dozen or more companies looking to possibly buy it. Increasingly, the company looking to sell itself hires an outside expert to do a single analysis and makes that analysis available to all potential buyers, so that each potential buyer does not have to hire its own analyst to assess the potential purchase. This makes the process easier for the company to be sold, since there are not experts from one or another potential buyer continually running around the business interfering with the work being done.

CHAPTER ONE

The Business Plan

It felt like it was time to update this book. We called our publisher, John Wiley & Sons, and discussed the ideas we had for a new edition. Wiley “did” a business plan. It may not have been written in the format suggested in this book, but make no mistake, before the company agreed to a new edition, it analyzed the competitive marketplace, determined if it could get a fair return on investment, looked at the credibility of the authors, and decided to invest in the new edition. This is exactly what any potential investor does when reading a business plan.

Keep in mind that entrepreneurs are most often doers rather than proposal writers. They would rather be on the battlefield—the cutting edge of business—than behind the lines planning their assault. They always want “to get on with it.” In addition, many entrepreneurs have difficulty articulating the business concepts that have often become second nature to them. They cannot find a way to share their vision in a manner that is conducive to some of the important sponsors of their project.

The same entrepreneur who can rally his team of employees to achieve breathtaking accomplishments often cannot sell the idea to the capital markets. The entrepreneur’s personal confidence in the venture may be enough to get early investors and key employees on board, but not enough to convince others who do more thorough due diligence before investing. With so many ventures seeking funding, translating ideas and personal qualities

into the format needed by a potential investor or lender is not always easy.

We once worked with an entrepreneur who had what we all thought was a great idea. He saw a need for a single store with carpet, lighting appliances, window treatments, paint, cabinets, tile, and other “home interior” items. It was a great idea. Today, we see this idea alive in many “home stores” including the Home Depot and the Lowe’s stores.

Our entrepreneur friend said the store needed to be a place where men are comfortable. He was right. He had developed this concept after working with a major paint company. He said it has to be all pulled together. He had a team ready to go from each potential department. He knew the vendors. He had scouted out locations in which to run pilots. He had assurances from a team of executives.

He could not, however, get funded! His vision was so clear to the believers on his team and his advisers that no one saw the need to put it all down on paper in order to make a cohesive presentation to possible investors. He preferred extemporaneous conversation to the structured approach. Even use of the business plan concept as an outline for the presentations may have helped. A business plan may have allowed “teaming” with others, who could have helped raise the necessary funds. Many less significant opportunities get funded.

Consequently, one of the most difficult chores they face is the preparation and actual writing of a business plan. Whatever difficulty the preparation of a business plan may present, a plan is an absolute necessity for any business.

A business plan serves three functions:

1. Determining future projects
2. Determining how well goals have been met
3. Raising money

First and foremost, it is *a plan* that can be used to develop ideas about how the business should be conducted. It is a chance to refine strategies and “make mistakes on paper” rather than in the real world, by examining the company from all perspectives, such as marketing, finance, and operations.

Second, a business plan is a retrospective tool against which a businessperson can assess a company’s actual performance over time. For example, the financial part of a business plan can be used as the basis for an operating budget, and can be monitored carefully to see how closely the business is sticking to that budget.

In this regard, the plan can and should be used as the basis for a new plan. After some time has elapsed, and thereafter on a periodic basis, the business plan should be examined to see where and even why the company strayed, whether that straying was helpful or harmful, and how the business should operate in the future.

The third reason for writing a business plan is the one most people think of first, that is, to raise money. Most lenders or investors will not put money into a business without seeing a business plan. There are stories of wild-eyed entrepreneurs and venture capitalists with pens at the ready who meet, scribble some projections on a wet cocktail napkin, shake hands, and become “partners” in a hot technology business, but most of those stories are urban legends.

Even during the earlier years of the modern venture capital boom—during the mid and late 1970s—and again in the

days of “irrational exuberance”—during the late 1990s—when there may have been less formality and more dynamism in the venture capital world, there was always an orderly process for securing venture capital. A large part of that process is the preparation and examination of a business plan.

If an entrepreneur presents an idea to a commercial lender or a potential investor without a business plan in hand, that money source will ask the entrepreneur to draft one and come back later. Or worse, the potential source of money may not take the entrepreneur seriously, and may not ask the entrepreneur back at all. Assuming that he or she invites the entrepreneur back, the entrepreneur may wish to seek professional assistance in writing the plan, perhaps from a consultant or an accountant. The bottom line, however, is that a formal, written plan must be prepared if the venture and the funding request is to be taken seriously.

A business plan is a document designed to map out the course of a company over a specific period of time. Many companies write annual business plans, which focus intently on the coming 12 months and give more general attention about the following one to four years. Few business plans project beyond five years.

Because the business plan is a hybrid document—part pragmatic projection and part sales tool—it must walk a fine line in content and tone of presentation. The information must be accurate, yet must convey a sense of optimism and excitement. Although risks must be acknowledged, they should not be dwelled on.

The tone should be businesslike. If there is too much form over substance, people won’t take the plan seriously. But

the people who read business plans are real people. They respond to positive, interesting presentations, and are turned off by those that are vague, long-winded, or not well thought out and organized. They may also read so many business plans in a week that their eyes glaze over.

Therefore, a business plan that makes especially good use of graphics, or that paints a picture of the company in a provocative way, has a better chance of being looked at closely than one that is monotonous and gray. Even minor errors in spelling and grammar can suggest substantial negatives regarding the entrepreneur and therefore the entire enterprise. Have someone skilled in this area review the plan to eliminate these minor annoyances that may have a major impact on the reader.

Many people we meet already have experience writing a business plan and do not even realize it. Everything that is done in business and, for that matter, in life has an inherent business plan aspect associated with it. We're fond of saying that even the publishing of this book was the subject of a business plan. The publisher, John Wiley & Sons, had to see if the book met the needs it had for the marketplace it serves. Wiley had to look at the economics associated with this book and see if it wanted to invest the time and resources necessary for publication. Similarly, the executives from Ernst & Young, who are usually serving clients, had to look at the time and energy and expense associated with the publication and determine that it met various goals that were important to Ernst & Young and to those individuals. Business plans are everywhere!

SPECIAL EXHIBITS AT THE FRANKLIN INSTITUTE

Virtually every endeavor an organization undertakes has an inherent business plan nature. Dennis Wintz is an extraordinary executive who has done an excellent job of providing leadership to the Franklin Institute in Philadelphia, founded by one of the most important entrepreneurs in this country's history, Benjamin Franklin.

Dennis has been incredibly successful at reengineering the Institute's offerings. He has brought a number of wonderful traveling exhibits that have accomplished numerous purposes. In addition to funding themselves and providing some funds to offset general operating and capital needs, these "blockbuster" exhibits have also increased the esteem with which the community holds this important institution. What was once thought of by many as a stodgy museum of history is now considered a dynamic institute of knowledge.

In every instance when an exhibit is brought to the institute, a business plan is developed to consider each aspect of the exhibit. In addition to an operating budget, there are considerations for all of the essential elements discussed in this book. These include marketing and promoting the exhibit; the human resources necessary to manage and administer all aspects of the project; capital budgets to make the necessary physical adjustments to the facility to house the exhibit; and consideration of the exhibit logistics, such as hours, special entrances to the space from the general exhibit hall, exhibit security, and so on.

Each special exhibit is, in effect, a new business in the “portfolio” of the Franklin Institute.

PLANNING NEEDS TO BE DYNAMIC

Even when typewriters were still in vogue, a friend said that Rule 1 for preparing a business plan is, “Do it on a word processor.” Another colleague always packages business plans in a three-ring binder. The message is clear. Business plans are ephemeral; they are constantly subject to change and adjustment. The preparation of a business plan must be seen as an iterative process, as both the assumptions and the projections those assumptions engender must be constantly refined. And the preparation of a business plan never really stops.

It usually takes months to obtain financing. While financing can be closed in as little as three months, this is the speed of light in the business world, and six or more months is often more realistic. Some potential sources of funding may want to see updates of the plan, fresh thoughts, or updated financial figures if the company is already doing business.

While a company may formally rewrite a business plan every year, it may want to monitor and update the plan more frequently, perhaps quarterly or even monthly.

LOOKING FORWARD—THE BUSINESS PLAN AS A PLANNING DOCUMENT

Many people who think “business plan” think “start-up company.” Yet this is not necessarily accurate. Ongoing companies should and often do create business plans.

For an ongoing business, the business plan serves a number of functions. It is a way of getting consensus and

consistency throughout the company. While business plans of rank start-ups are often written by one or two people, in an ongoing company—especially one that is larger—a number of people will have a hand in writing the business plan.

By the time the business plan has run through a number of revisions and is produced in final form, a large number of people will have been involved in preparing the plan's vision for the company.

A frequent complaint from those running existing small businesses is that, because of the day-to-day management pressures involved in a small company, there is precious little time for planning. This is, of course, unfortunate, since a continuing effort at business planning is probably more important to the survival of a small company than to a large company.

The business plan is, in many ways, a company's first crack at strategic planning. And, contrary to what many people think, strategic planning not only *can* be done in the context of a small company, but it is vital, as a small company often does not have the resources that allow it to recover from mistakes.

The business plan is also an implementation tool. It can be used to test theories of how the company should be run and to calculate possible outcomes. Then the plan can be checked as those ideas are implemented to see if the projections were accurate. This step provides an early-warning system and allows for prompt action to correct problems.

Ongoing companies or those acquiring existing businesses have an advantage over new companies when developing a business plan. The numbers they use to make projections will have some basis in fact and experience. And the

strategies they outline for the business's future are also rooted in their past strategies, incorporating what the company gained from its successes and learned from its mistakes.

Many of the questions one needs to ask to prepare a business plan must be successfully answered, or at least put in the "can't be answered at this time but must be monitored" folder, if a company is going to survive.

Sometimes, a key question is overlooked. For instance, a promising small specialty chemical company forgot to ask itself about the impact of federal environmental regulations before starting up its business. The company went into production in 1983, anticipating the first sales in 1984. It hired personnel, opened an office, and began marketing. With the meter running—the company was incurring significant overhead—the company finally discovered that it would need a federal Environmental Protection Agency (EPA) review of its products before it could actively market them. The company nearly bled itself dry maintaining its facilities and personnel while its product was tied up in review. This particular company made it, but others aren't so lucky.

Another company's business plan was good enough to acquire financing. The company was going to provide technical studio facilities for the production of audio and video products.

On the level of a business concept, the plan was good. But it lacked the depth necessary to make it a good implementation plan. After difficult negotiations relative to financing, the deal was finally closed in November. The company's owner told his consultant to expect an invitation to a February grand opening.

“Doesn’t February sound a little quick?” the consultant asked the owner. “Shouldn’t you sit down and draw up a more detailed implementation plan?” The owner had a lot of equipment to buy, personnel to hire, and marketing to do. Some city approvals were also required.

“Don’t worry,” the owner said. He felt he knew what he was doing.

The grand opening was held in May. It was beautiful, but it was also the company’s last hurrah. The owner had planned to have \$125,000 in working capital when the business opened. But after being delayed for four months, and after throwing the lavish party, he was practically tapped out.

The lesson here is that anytime there is a dynamic situation, there should be a business plan. If there are unaccounted-for variables, they should at least be acknowledged and noted.

Exxon lost millions of dollars in the office products business. So did Digital Equipment Corporation in the personal computer business. Companies that size can survive debacles and go on to future successes, but small companies can’t. They need to plan carefully.

SUCCEEDING BY SUCCEEDING, SUCCEEDING BY NOT FAILING

There are those who succeed by succeeding. They have some kind of “magic”—persistence, gumption, the willingness to roll the dice and the luck to have it come up seven—that can’t be taught; or if it can, it can be taught only over many years. Some people are almost destined to succeed because of past success. Entrepreneurs with track records of success get significant attention paid to their

plans, and often get the benefit of the doubt in organizing a venture.

Although succeeding by succeeding can't be taught except through years of experience, succeeding by not failing can be. This, in many ways, is the heart of business planning.

There are a number of key hurdles in the creation of any business, each of which can result in disaster if improperly addressed. These include developing management and support employees, raising capital, developing and marketing product, keeping margins acceptable, and dealing with outside influences. Depending on which statistics one uses, 75 percent of all new businesses fail in the first few years, most for one of these reasons. A few are attacked by "factor x," the unpredictable (see [Figure 1.1](#)).

At each one of these hurdles, an entrepreneur must examine the business, ask questions, and ferret out the possible problems. Each time a businessperson identifies a problem and solves it, he or she eliminates one more variable that can cause failure, and increases the chances of success.

Through careful planning, most problems can be solved. By doing careful planning and solving all the problems that can be solved, a businessperson can, in effect, stack the deck in favor of success.

LOOKING BACKWARD—THE BUSINESS PLAN AS A YARDSTICK

The constant updating of the business plan helps the plan fulfill its second major purpose, that of being a yardstick against which to measure the company's actual performance.

Last year's business plan can tell a company what strategy was effective or ineffective and what implementation was effective or ineffective.

Simplicity is a virtue to the extent that it eases implementation. However, often what looked simple on paper when the previous business plan was being prepared became complex in implementation. Examining the business's actual performance against the business plan can identify strengths and weaknesses in the organization—sometimes relating to people—that separate strategy from effective implementation.

This chart reflects the relationship between business failure and success for new enterprises. The shaded area reflects failure. This area is further divided into wedges that identify functional areas into which costly mistakes may be categorized. The three-to-one ratio of failure to success is probably not far from reality. While each wedge in the shaded area is equal in size and thus does not reflect a statistically accurate representation of the proportion of failures attributable to a particular functional area, it is instructive. To the extent that the entrepreneur addresses each functional area in a way that reduces the probability of costly error, the odds increase that the venture will be one of the fortunate ones that end up in the white (success) area.

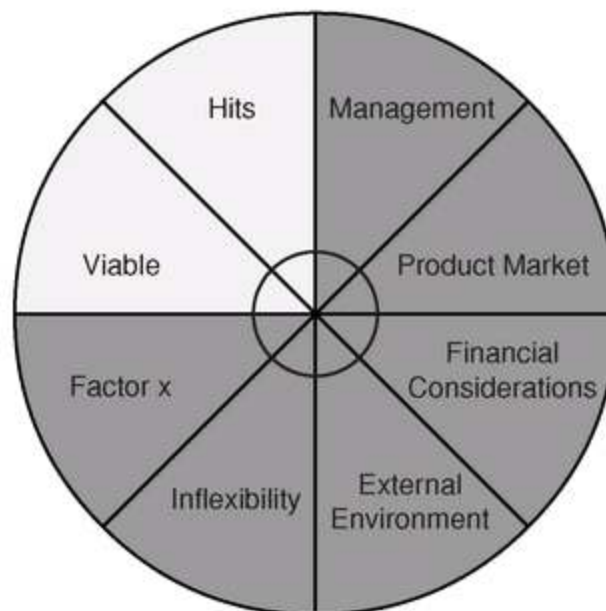


FIGURE 1.1 SUCCEEDING BY NOT FAILING (HALF OF THE FORMULA FOR SUCCESS)

The financial section of the previous business plan can be used in an objective, concrete way to monitor the business's performance. The financial projections made when the plan was drawn up became the basis for the budget under which the company tried to operate. Deviations from that budget point out areas where either necessary resources were misjudged or possibly controls were lax during the period the business plan encompassed.

In addition to management, others will use the business plan as a monitoring tool. Financial sources, both lenders and investors, will note deviations between the plan and the company's actual performance; they will also ask why those deviations occurred. They may ask the question in a cordial manner, as part of a meeting to draw up the next business plan. Or they may ask the question as they are telling the businessperson to pack his or her bags and hand over the key to the restroom door, pursuant to the terms of the lending or investing agreement.

This is one of the arguments against overly hyping a business in a business plan. Professionals—consultants, accountants, and lawyers who work with businesspeople in writing business plans and securing financing—often counsel their clients to make realistic projections. Why should an entrepreneur aspire to be “superhuman” and risk not meeting projections when a little more modesty will produce projections that can much more easily be attained—or even exceeded—thereby keeping lenders happy and still providing investors with a healthy rate of return?

RAISING CASH—THE BUSINESS PLAN AS A FINANCING TOOL

This is the role of a business plan most people think of first. While we list this role last, it, too, is critical. After all, if a